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Supreme Court of the United States

October Term, 1965

No. 2[redacted]463

IN THE MATTER
OF
J. E. SCHECTER CORPORATION,
Petitioner,
AND
CARRIER CORPORATION, AMERICAN RADIATOR & STANDARD SANITARY CORPORATION, SARCO COMPANY, INC. and SARCOTHERM CONTROLS, INC.,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Supreme Court of the United States

OCTOBER TERM, 1965

No. 29,458

In the Matter

of

J. E. SCHECTER CORPORATION,

Petitioner,

AND

CARRIER CORPORATION, AMERICAN RADIATOR & STANDARD SANITARY CORPORATION, SARCO COMPANY, INC. and SARCOTHERM CONTROLS, INC.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The petitioner, J. E. Schecter Corporation, debtor in possession, prays to this Court that a Writ of Certiorari issue to review the judgment and decree of the United States Court of Appeals for the Second Circuit, which decision reversed the order and judgment of the United States District Court for the Eastern District of New York and the order and decree of the Referee in Bankruptcy.

Jurisdiction

The judgment of the United States Court of Appeals, Second Circuit, sought to be reviewed, was entered on May 21, 1965. The jurisdiction of this Court is invoked under 28 U. S. C. Section 1254(1), and Section 24c of the Bankruptcy Act, 11 U. S. C. Section 47c.

The Opinions Below

The opinion and order of the Referee in Bankruptcy is reproduced in the Appendix of the Court of Appeals 31a through 39a. The opinion of the United States District Court for the Eastern District of New York, which upheld the decision of the Referee in Bankruptcy and the contentions of the petitioner herein, is set forth in 234 F. Supp. 474. The opinion of the Court of Appeals for the Second Circuit, which reversed the decision of the United States District Court and the decision of the Referee in Bankruptcy is reported in —— F. 2d ——.

Questions Presented for Review

The questions presented by this petition are as follows:

1. Did the Court of Appeals for the Second Circuit err in reversing the United States District Court and Referee in Bankruptcy by impressing a trust on funds in the hands of the petitioner in light of established New Jersey statutory and case law?

2. Is the decision of the United States Court of Appeals in conflict with recognized Federal jurisprudence as established by Section 1652 of Title 28 of the United States Code and the principle of *Erie* v. *Tompkins*?

3. Does the force of New Jersey criminal statute 2A:-102-11 relating to private improvements give rise to a civil remedy permitting the impression of a trust in light of established New Jersey statutory and case law?

Statutes Involved

Criminal Statutes of New Jersey

"Embezzlement, Conversion and Misappropriation."

"2A:102-10. Misappropriation of funds paid to contractor for building purposes.

All moneys received by a contractor from the owner or mortgagee of real estate or any leasehold or other interest therein, for the purpose of having a building erected, constructed, completed, altered, repaired or added to, are trust funds in the hands of the contractor to be applied to the amount of all claims due or to become due and owing from the contractor to all persons furnishing labor or materials to him for the erection, construction or completion of the building or any alteration, repair or addition thereto, and any other reasonable and necessary charge in connection therewith. Any contractor or any officer, director or agent of the contractor, who pays or consents to the appropriation of such funds for any other purpose prior to the payment of all claims and charges for the payment of which the funds constitute a trust fund, is guilty of a misdemeanor. As amended L. 1954, c. 123, p. 599, Section 1."

"2A:102-11. Misappropriation of funds paid to subcontractor for building purposes.

All moneys received by a subcontractor from the owner or mortgagee of real estate, or any leasehold or other

interest therein, or from a contractor, for the purpose of having a building erected, constructed, completed, altered, repaired or added to, are trust funds in the hands of the subcontractor to be applied to the amount of all claims due or to become due and owing from the subcontractor to all persons furnishing labor or materials to him for the erection, construction or completion of the building or any alteration, repair or addition thereto, and any other reasonable and necessary charge in connection therewith. Any subcontractor, or any officer, director or agent of the subcontractor, who pays or consents to the appropriation of such funds for any other purpose prior to the payment of all claims and charges for the payment of which the funds constitute a trust fund, is guilty of a misdemeanor. As amended L. 1954, c. 123, p. 599, Section 2".

"2A:102-12. Misappropriation of funds received by contractor for construction of public improvement.

All moneys paid by the state, or an agency, commission or department thereof, or by a county, municipality or school district, or by a public authority, to any person pursuant to the provisions of a contract for the making of any public improvement, shall constitute a trust fund in the hands of such person as contractor. Any such person who shall use any of the moneys so received for a purpose other than the payment of claims for labor or material and such other proper charges as are incurred in connection with the contract, is guilty of a misdemeanor." L. 1932, C. 269, Sub Section 1, 2, p. 605 suppl. to L. 1898, C. 235, p. 794.

"2A:102-12.1. Evidence; sufficiency to authorize conviction.

It shall be deemed to be sufficient evidence to authorize conviction under sections 2A:102-9, 2A:102-10, 2A:102-11

or 2A:102-12 of the New Jersey Statutes, if it shall be proved that any person:

(1) Received any moneys or funds, which under any of said sections are declared to be trust funds in his hands for the purpose in said section described, and

(2) Failed to apply such moneys or funds, to any of the purposes to which they are provided by said section to be paid or applied;

unless it appears from the evidence against him that he has not paid or consented to the payment or appropriation of any such moneys or funds in any manner contrary to that prescribed in said section: L. 1959, c. 98, p. 238, Section 1."

Civil Statutes of New Jersey, Chapter 44

"Liens—Bonds of and Money Paid to Contractors on Public Works"

"Article 13. Money Paid to Contractors on Public Improvements as Trust Fund.

2:A44-147.* Money paid to contractor trust fund for payment of claims.

All money paid by the state of New Jersey or by any agency, commission or department thereof, or by any county, municipality or school district in the state, to any person pursuant to the provisions of any contract for any public improvement made between any such person and the state or any agency, commission or department thereof, or any county, municipality or school district in the state, shall constitute a trust fund in the hands of such person as such contractor, until all claims for labor,

* Should be 2A:44-148.

materials and other charges incurred in connection with the performance of such contract shall have been fully paid."

Statement of Case

The petitioner is a debtor in possession following the filing of a petition for an arrangement pursuant to Section 322 of Chapter XI of the Bankruptcy Act on November 27, 1962.

The respondents are suppliers of air conditioning, heating and ventilating equipment, who supplied the petitioner with such equipment for the improvement of a private improvement known as the "Engineering Quadrangle" at Princeton University, Princeton, New Jersey. The petitioner contracted with William L. Crow Construction Co. for the construction of heating, ventilating and air conditioning work for the "Engineering Quadrangle" for the sum of $1,223,970.

On December 16, 1963 the respondents as alleged Trust beneficiaries moved before the Referee for an order directing payment by the petitioner to the respondents and other job claimants of funds derived by petitioner from the "Engineering Quadrangle" construction contract, and for legal fees to the attorneys for the respondents.

The petitioner opposed the application on the grounds that the law of New Jersey was applicable to the funds in question and that Section 2A:102-11 of the Statutes of the State of New Jersey provided criminal penalties for misapplication of trust funds resulting from an improvement to real property, rather than civil remedies, and that the claims of the respondents were barred by the Statute of Limitation.

The Referee in bankruptcy denied the motion of the respondents and stated in his conclusions of law that "1. The Lien Law of the State of New York only applies to a contract for the improvement of real property located in the State of New York" and "2. That Section 2A:102-11 of the New Jersey Statutes is a criminal statute which provides no civil remedy for a diversion of funds received by a contractor for an improvement of real property located in the State of New Jersey." The Referee cited in support of his decision the case of *Plevy* v. *Schaedel*, 44 N. J. Super. 450, which held that New Jersey Statute 2A:102-10 created a criminal offense, but stated "no civil remedy was created by force of the criminal statute."

In the United States District Court, the respondents sought to review the decision of the Referee with respect to the trust fund issue and in the alternative to review the refusal of the Referee to order the return of a portion of the funds which the petitioner, pursuant to a prior order of the Referee, had paid to other creditors who had claimed some part of the funds from the New Jersey construction. The District Court in its decision upheld the Referee with respect to the issue of a civil trust fund and denied legal fees, but with respect to the payment made to other creditors, stated that the funds paid to said creditors were distributed improperly inasmuch as notice was not given to the requisite number of creditors, which included the respondents, and accordingly directed the petitioner to institute proceedings before the Referee to recover such funds from said creditors.

The respondents appealed to the Court of Appeals for a review of the decision of the District Court and the petitioner cross appealed from so much of the order of the District Court as required it to institute a proceed-

ing before the Referee for the recovery of the funds. The Court of Appeals reversed the Referee and the District Court and impressed a fund on "general equity principles" and directed that attorneys' fees for the respondents be determined by the District Court and be paid from the trust funds. With respect to the cross appeal by the petitioner, the Court declared the question as moot by reason of the fact that a Trust was impressed. The Court of Appeals reiterated the position of the Referee and the District Court that the laws of the State of New Jersey were applicable to the within matter rather than the laws of the State of New York.

The petitioner agrees that New Jersey laws govern the instant matter rather than the laws of the State of New York. However, petitioner deems the opinion and judgment of the Court of Appeals in conflict with accepted federal jurisprudence as well as the established statutory and case law of the State of New Jersey.

Reasons for Granting the Writ

The brief in support of this petition points up the fact that the decision of the Court of Appeals conflicts with the decision of the Courts of the State of New Jersey and further conflicts with the applicable statutes enacted in the State of New Jersey with respect to funds derived by a contractor from the construction of private improvements. It is respectfully submitted that the Court of Appeals was required by the decision of *Erie* v. *Tompkins*, 304 U. S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, and Title 28, Section 1652 of the United States Code to apply the established law of the State of New Jersey, when it found that the law of New Jersey governed the within matter. The cases relied upon by the Court of Appeals with respect

to New Jersey law were applicable only to *public* improvements in the State of New Jersey, and were not applicable to funds received by a contractor from *private* improvements. The cases cited by the petitioner and the applicable statutes with respect to New Jersey law established the law of New Jersey, and the Court of Appeals was bound to accept such law as controlling.

The instant matter is of utmost importance since it concerns the right of the Federal Court to determine a matter on "general equity principles" which find no basis in the applicable laws of the State of New Jersey. Having determined that the law of the State of New Jersey applied, the Federal Courts are required to enforce the statutory and case law of that State.

ARGUMENT

POINT I

Federal courts are bound by state substantive statutes and related decisions.

Erie v. *Tompkins*, 304 U. S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, binds the Federal Courts to recognize and enforce the statutes and decisions of the sovereign states in regard to matters of substantive law. In addition to the foregoing, Title 28 of the United States Code, Section 1652, entitled "State Laws as Rules of Decision" provides as follows:

> "The laws of the several states, except where the Constitution or treaties of the United States, or Acts of Congress, or otherwise, require or provide, shall be regarded as rules of decision in civil

actions in the courts of the United States in cases where they apply."

In *Brady* v. *State of Maryland*, 373 U. S. 83, 83 S. Ct. 1194, 10 L. Ed. 2d 215, this Court stated that:

"State courts, state agencies and the state legislatures are final expositors of state law under our federal regime."

The decision of the Court of Appeals is in direct conflict with established New Jersey law. In failing to apply the statutes of the State of New Jersey and the cases construing such statutes, and by utilizing "general equity principles," the Court circumvented the doctrine of *Erie* v. *Tompkins, supra.*

In *Krause* v. *Greenbarg*, 137 Fed. 2d 569 (3 Cir. 1943; cert. den. 64, S. Ct. 207, 320 U. S. 791), the Court stated:

"Our duty is to apply state law as we find it in the state decisions irrespective of what we may regard as its merits."

In *Yoder, et al.* v. *Nu-Enamel Corporation*, 117 F. 2d 488 (8 Cir. 1941), the Court stated:

"In the application of a state statute, the federal courts are, of course, bound by the construction made by the courts of the state. Senn v. Tile Layers Union, 301 U. S. 468, 57 S. Ct. 857, 81 L. Ed. 1229. And the obligation to accept local interpretation extends not merely to definitive decisions, but to considered dicta as well. Hawks v. Hamill, 288 U. S. 52, 53 S. Ct. 240, 77 L. Ed. 610; Badger v. Hoidale, 8 Cir., 88 F. 2d 208, 109 A. L. R. 798. Indeed, under the implications of Erie Railroad

Co. v. Tompkins, 304 U. S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, 114 A. L. R. 1487, and West v. American Telephone and Telegraph Co., 61 S. Ct. 179, 85 L. Ed. —., where direct expression by an authorized state tribunal is lacking, it is the duty of the federal court, in dealing with matters of either common law or statute, to have regard for any persuasive data that is available, such as compelling inferences or logical implications from other related adjudications and considered pronouncements. The responsibility of the federal courts, in matters of local law, is not to formulate the legal mind of the state, but merely to ascertain and apply it. Any convincing manifestation of local law, having a clear root in judicial conscience and responsibility, whether resting in direct expression or obvious implication and inference, should accordingly be given appropriate heed."

See also:

Shealy v. *Challenger Mfg. Co.*, 304 F. 2d 102 (4 Cir. 1962).

The Court of Appeals has departed from required standards of Federal jurisprudence in applying "general equity principles" to a factual situation governed by state statutes and the decisions construing those statutes.

It is necessary and important that this court review decisions which are at variance with Title 28, Section 1652 of the United States Code.

POINT II

The statutory laws of the State of New Jersey provide no civil remedy for the impressing of a trust on funds obtained by a contractor arising from the construction of a private improvement.

Petitioner contends that solely by force of statutory enactment can a trust be impressed in the instant matter. New Jersey enacted specific legislation concerning funds derived by a subcontractor involving construction of public and private improvements. Section 2A:102-10 and Section 2A:102-11 of the New Jersey Statutes enunciate criminal statutes with respect to contractors and subcontractors and contain the same language.

Petitioner was a subcontractor performing certain services on a private improvement known as the "Engineering Quadrangle" at Princeton University, in Princeton, New Jersey. It is conceded by both petitioners and respondents that such construction related to a private improvement.

The aforesaid statutes, together with Sections 2A:102-12 and 2A:102-12.1 are clearly criminal in scope and purpose and are found in the sections of the New Jersey Statutes relating to embezzlement, conversion and criminal justice. The respondents contend that Sections 2A:102-10 and 2A:102-11 create civil remedies for the impression of a trust on funds in the possession of the petitioner. The petitioner contends that the aforesaid statutes are wholly criminal in nature and scope and that there is no civil remedy by force of the criminal statutes.

It is without dispute that Sections 2A:102-10 and 2A:102-11 relate to funds in the hands of a contractor or

subcontractor resulting from the construction and improvement of property of a private nature and that Section 2A:102-12 is a criminal statute relating to funds derived by a contractor for the improvement of property of a public nature. Section 2A:102-12.1 sets forth the criteria to authorize criminal convictions with respect to Sections 2A:102-10-11 and 12.

With respect to the Criminal statute dealing with public improvements, as cited in New Jersey Statutes Annotated, at page 173, the following appears "Cross Reference": "Money paid to contractor as trust fund. See Section 2A:44-148."

With respect to the private improvement criminal statute, at page 173 of the same volume, appears the following "Cross References" with respect to Section 2A:102-11: "Punishment for misdemeanor. See Section 2A:85-7."

On page 569 of the New Jersey Statutes Annotated, wherein Section 2A:44-148 appears, the following "Cross Reference" is indicated: "Misappropriation as misdemeanor, see Section 2A:102-12."

The Legislative history of Sections 2A:102-12 and 2A:102-10-11 indicate that said laws were enacted by the same Legislature of the Senate and General Assembly of the State of New Jersey in 1932. In April of 1932, the forerunner statutes of 2A:102-10 and 2A:102-11 were enacted. On June 15, 1932, the Legislature enacted the forerunner of Section 2A:102-12 and the forerunner of Section 2A:44-148. It is of significance that the same New Jersey legislature enacted both the public and private improvement statutes and that said legislature also enacted a civil counterpart limited to the public improvement statute.

The petitioner contends that the Court of Appeals erred in impressing a trust on the funds in the hands of the petitioner derived from a private improvement construction project, whereas the respondents contend that both on equitable principles and by a reading of Section 2A:102-10 and 11, the Legislature created both a criminal and civil trust fund remedy with respect to private improvements, thus permitting the impression of a civil trust on funds in the hands of the petitioner. As further evidence of the fact that no civil counterpart was enacted in New Jersey for private improvements, petitioner refers the Court to the various captions under which the aforesaid sections have been placed in the New Jersey statutes. It becomes apparent that Sections 2A:102-10, 11, 12 and 12.1, which appear under Ch. 102 of the New Jersey Statutes have been grouped with the criminal statutes under the heading of *"Embezzlement, Conversion and Misappropriation"*, whereas, Sections 2A:44-148 appear under Ch. 44 of the New Jersey Statutes entitled, *"Liens—Bonds of and Money paid to Contractors on Public Works"*. Article 13 which appears as a subdivision under Ch. 44 is entitled *"Money paid to Contractors on Public Improvement as Trust Fund"*. Therefore, in the enactment of public and private improvement trust fund statutes, the Legislature well knew the purport of its acts since it saw fit to enact a civil counterpart to the provisions relating to public improvements and placing said law with other statutory civil lien laws but did not enact a civil counterpart to the criminal private improvement statutes.

The Courts of the State of New Jersey have made clear the intention of the Legislature with respect to each of the above statutes and by no force of judicial construction in light of the background of the enactment of the

aforesaid statutes could the Court of Appeals have construed a remedy permitting the impression of a trust on the funds in the hands of the petitioner with respect to private improvements.

POINT III

Case law of New Jersey is dispositive of the issue and reenforces the petitioner's contention herein.

Each of the statutes referred to in Point II of this petition, with the exception of 2A: 44-148, imposes a criminal penalty upon a subcontractor or contractor who diverts funds with respect to either public or private improvement construction, but only Section 2A:102-12 imposes a civil remedy for the recovery of the funds by virtue of 2A:44-148.

The cases of *Plevy* v. *Schaedel,* 44 N. J. Super. 450, 452, 130 A. 2d, 910 and *Samuel D. Wasserman* v. *Klahre,* 24 N. J. Super. 143, 93 A. 2d 628, are dispositive of the issue as to whether or not the private improvement criminal statutes create a remedy for the recovery of such funds.

In the *Plevy* case, the plaintiff, a subcontractor, brought an action against Schaedel for damages arising from a breach of contract. Schaedel was a New Jersey contractor, under contract to furnish certain repair work on a private improvement in the State of New Jersey. The owner of the property paid Schaedel pursuant to the general contract. Thereafter Schaedel was adjudicated a bankrupt and the plaintiffs were not fully paid for the work done as a subcontractor. Plaintiffs contended that they had a right of action to impress a trust under New Jersey Statute 2A:102-10.

The facts stated in such case are similar, if not exactly in point to the facts of the within matter. The Court stated:

> "Waugh, J.S.C. The sole question to be decided in this case is whether or not N.J.S. 2A:102-10 creates a civil remedy available to the plaintiffs."

The Court then went on to state:

> "Plaintiffs here urge that the use of the term 'trust fund' in this criminal statute creates a right inuring to his benefit whereby he can now proceed against the defendants in a civil action to recover the monies allegedly held in trust and wrongfully paid out prior to the satisfaction of his claim as sub-contractor against the defendant contractor.
>
> (1) I do not agree with plaintiffs' contention, and accordingly find that no civil remedy was created by force of the criminal statute. In reaching this conclusion, I find support in the case of Wasserman, Inc. v. Klahre, 24 N. J. Super, 143, 147 (App. Div. 1952), wherein the following language was used by our Appellate Division:
>
> 'Under our former Constitution, as under our present one, the title of a statute operates as a limitation on the enacting clauses, so that a construction which would give the statute a direct effect beyond the object expressed in the title must be rejected * * *. It is entirely clear to us that the scope of the statutory provision on which the plaintiffs build their case, is limited to the creation of a criminal offense; and that no civil action can be based directly on the statute.'
>
> This statute was enacted by the Legislature as L. 1932, c. 104 and was entitled 'A supplement to

an act, entitled 'An act for the punishment of crimes' (Revision of 1898).'

The argument by plaintiff that a civil remedy, is created by N.J.S. 2A:102-10 is clearly refuted by the title of the original legislature enactment under the rule of the Wasserman case, supra. See also Raymond Concrete Pile Co. v. Federation B. & T. Co., 288 N. Y. 452, 45 N. E. 2d 496 (Ct. App. 1942), affirmed on reargument 290 N. Y. 611, 48 N. E. 2d 709 (Ct. App. 1943).

Additional support for the conclusion I reach is found by contrasting the legislative treatment of contracts for public improvements with contracts concerning private individuals.

N.J.S. 2A:102-12 provides that it is a dismemeanor for a contractor to misappropriate funds received by him for construction of a public improvement. These funds are specifically designated as trust funds and N.J.S. 2A:44-148 creates as a civil matter a trust fund in the hands of the contractor until all claims for labor, materials and other charges incurred in connection with the performance of a public contract shall have been fully paid. N.J.S. 2A:44-148 provides as follows:

'2A:44-147. Money paid to contractor trust fund for payment of claims'

All money paid by the state of New Jersey or by any agency, commission or department thereof, or by any county, municipality or school district in the state, to any person pursuant to the provisions of any contract for any public improvement made between any such person and the state or any agency, commission or department thereof, of any county, municipality or school district in the state, shall constitute a trust fund in the hands of such

person as such contractor, until all claims for labor, materials and other charges incurred in connection with the performance of such contract shall have been fully paid.

Clearly, in the instance of public improvements, the Legislature has created a civil remedy, which has its criminal counterpart in N.J.S. 2A:102-12. However, the Legislature has not enacted a statute creating the same civil remedy to accompany, as it were, the crime which it created in N.J.S. 2A:102-10.

I find that the failure of the Legislature to specifically create the civil remedy in the case of private contracts as it did where public contracts are involved (N.J.S. 2A:44-148) cannot be cured by judicial interpretation of the term 'trust funds' as found in the statute defining the criminal act. Since criminal statutes must be strictly construed, and further, since it is a long standing precept that civil remedies are not created in criminal laws, I find hat plaintiff has not established that the moneys held by the defendant here were trust funds held for the benefit of the plaintiff and others in his class. I, therefore, deny plaintiffs' motion for summary judgment and grant defendants' cross motion for dismissal of the complaint for failure to state a cause of action."

The Court, referred to the New York case of *Raymond Concrete Pile Co.* v. *Federation Bank and Trust Company,* 288 N. Y. 452, 43 N. E. 2d 486, affirmed on reargument 290 N. Y. 611, 48 N. E. 2d 709, construing Section 25-a of the Lien Law of the State of New York as being penal in nature, to be strictly construed and not subject to judicial amendment so as to enlarge its clearly defined scope

and purpose to impose civil liability. Section 25-a contained the following clause:

> "The funds received by a contractor for a public improvement are hereby declared to constitute trust funds in the hands of such contractor to be applied first to the payment of claims of subcontractors * * *."

However, the statute was construed to be wholly penal in nature and could afford no civil relief. Notwithstanding that the sections of the Lien Law required a liberal construction, the Court reiterated that the Lien Law did not authorize judicial amendment so as to enlarge the clearly defined scope and purpose of Section 25-a, which was penal.

The Court in the *Plevy* case, in reaching its decision with respect to there being no civil remedy by force of a criminal statute, referred to the *Wasserman* v. *Klahre* case, *supra,* wherein the plaintiff a materialman supplied to Candrilli certain materials and labor for the construction of a private improvement in New Jersey. Wasserman was not paid in full and the defendant, Klahre, who was a judgment creditor of Candrilli and unrelated to the construction of the private improvement in question had levied upon Candrilli's bank account, which had funds therein derived from the construction of the private improvement. Klahre obtained the money toward the satisfaction of his judgment against Candrilli and the plaintiff, Wasserman, instituted an action against Klahre pursuant to New Jersey Revised Statutes 2:124-16 which was the forerunner to 2A:102-10 on the basis that Klahre was in the possession of trust funds that rightfully belonged to Wasserman. The question presented to the Court was whether or not the money in the hands of

Klahre constituted a trust fund and the Court, in reaching its decision in favor of the judgment creditor against the impressing of a trust, stated as follows:

> "(1) 'In the absence of statute, one who furnishes material or labor for a building or any structure which is part of the land has no lien, legal or equitable, on the land, the structure, or the contract price.' Guise v. John C. Guise, Inc., 116 N. J. Eq. 590 (E. & A. 1934). And see Grover v. Board of Education, 102 N. J. Eq. 415 (Ch. 1928), affirmed 104 N. J. Eq. 197 (E. & A. 1929).
>
> (8) The plaintiffs had a complete remedy under the Mechanic's Lien Law, R.S. 2:60-105, et seq., which they voluntarily surrendered when they executed and delivered discharges of their notices of intention and releases of their lien claims. * * * "

The respondents had enforceable civil remedies available to them by New Jersey statute. Pursuant to Article 10 of Chapter 44 of Title 2A of the New Jersey statutes, more particularly Sections 2A:44-64 through 2A:-44-124, the respondents could have filed a mechanic's lien against the property or a stop notice against the owner of the property pursuant to the "Mechanic's, Materialmen and Laborers in General" statutes.

2A:44-66 of the New Jersey statutes provides as follows:

> "Except as otherwise provided in this article, the property herein enumerated shall be liable for the payment of any debt contracted or owing to any person for any of the purposes herein specified, which debt shall be a lien upon such property; that is to say

> a. Every building together with the land whereon it stands, including the lot or curtilage whereon the same is erected, for labor performed or materials furnished for the erection, construction or completion of such building, or any alteration or repair thereof or addition thereto; * * *."

In *Friedman* v. *Stein*, 4 N. J. 34, 71 A. 2d 346, 1950, the Court stated:

> Mechanic's and materialmen's liens have no recognition in equity except as prescribed by statute, and being in derogation of common law, provisions of statute giving rise to such liens are to be strictly construed, while provisions for their enforcement are to be liberally construed.
>
> Mechanic's and materialmen's liens are distinct from underlying debts and liens afford a cumulative remedy for enforcement of debt, and claimant's status is that of a general creditor until those things are done which give him security of statutory lien and until then, lien is inchoate.

In addition to the filing of a mechanic's lien against the property, the law provides in Section 2A:44-77 for the issuance of "stop notices" where a contractor or subcontractor refuses to pay any person who has furnished him materials for use in or about the erection, construction, completion or repair of any building. The effect of such stop notices creates a fund from the owner of the property to the unpaid materialmen. After a stop notice is received by the owner and filed by the unpaid materialmen, the owner of the building is authorized to retain the amount which may be due the defaulting contractor and

may pay such sum to the unpaid materialmen in the same order as the stop notices are received.

In *Brown* v. *Home Development Co.*, 129 N. J. Eq. 172, 18 A. 2d 742, 1941, the Court indicated that a stop notice served on an owner of property by laborers and materialmen operated as an assignment *pro tanto* of the contract price owing by the owner to the contractor. The owner was obliged to retain, for the benefit of those unpaid materialmen giving notice, all funds which might thereafter become payable to the defaulting contractor under the contract. See also *Tile Wholesalers & Importers* v. *Ruppert*, 125 N. J. L. 597, 17 A. 2d 607, 1941.

The respondents had an adequate statutory remedy to enforce the collection of any unpaid sums due them from the petitioner. However, respondents apparently failed to take advantage of such statutory remedies and now seek to create a civil remedy which is unknown in the State of New Jersey.

POINT IV

The cases relied upon by the Court of Appeals are not dispositive of the issue.

In the lower Court the respondents urged that the decisions in:

Albert Pick Co. v. *Travis*, 6 F. Supp. 486 (E. D. N. Y. 1933);

In re Heintzelman Const. Co., 34 Supp. 109 (W. D. N. Y. 1940);

Wickes Boiler Co. Inc. v. *Godfrey-Keeler, Inc.*, 116 F. 2d 842 (C. C. A. 2d, 1940), mod. 121 F. 2d 415, cert. den. 314 U. S. 686.

were controlling with respect to the within matter. It is respectfully submitted that the aforesaid cited cases have three characteristics in common which distinguish them from the instant matter:

(1) New York State law was applied by the Courts;

(2) Section 36-a of the Lien Law of the State of New York was the subject of each of the cases which involved private improvements;

(3) Section 36-a of the New York Lien Law constitutes a criminal and civil statute.

In each of the above cited cases the plaintiff was engaged as a subcontractor or contractor dealing in the State of New York pursuant to Section 36-a of the Lien Law of the State of New York. The statute in question was construed to be both criminal and civil in nature and the Court impressed a trust in favor of the subcontractor. These cases cannot be construed with the provisions of the New Jersey statutes which have been segregated into private and public improvement statutes of which only the public improvement statute has been held to create civil remedies by reason of a separate statutory enactment.

The cases cited by the respondent with respect to New Jersey law, to wit:

National Surety Corp. v. *Barth,* 11 N. J. 506 (1953);

Morris Picker v. *City of Bayonne, et al.,* 60 N. J. Super. 251;

Wilson v. *Robert A. Stretch, Inc.,* 44 N. J. Super. 52, 58;

Stulz-Sickles Co. v. *Friedburn Const. Corp.,* 114 N. J. Eq. 475;

are not dispositive of the issue since each of said cases involved public or municipal improvements under Section 2A:44-148 of the New Jersey Statutes. In said cases the funds created with respect to the public project were created by specific State and local public laws earmarked for specified purposes. In *National Surety Corp.* v. *Barth, supra,* the statutes involved related to funds for public housing. The Court stated:

> "Clearly funds have been appropriated and dedicated for a specific purpose by the United States Congress, The New Jersey Legislature and the voters of the State of New Jersey. A special fund labeled 'State Housing Fund' has been established and all monies deposited therein are earmarked for the purposes of emergency housing."
>
> "The Legislature clearly intended to set aside all monies received from these three sources and to earmark them for the purposes of public housing. The money was not available for any use except in furtherance of the policies of the act."

In *Morris Picker, supra,* the City of Bayonne, New Jersey constructed a municipal swimming pool by sale of bonds pursuant to the local bond law. The Court again referred to Section 2A:44-148 of the New Jersey Statutes and stated that a civil remedy was created with respect to the public improvement funds.

In *Stulz-Sickles Co., supra,* the subject matter of the suit related to funds due a contractor involved in municipal construction. Section 2A:44-148 was again involved and the Court permitted a civil remedy by reason thereof.

To enunciate a civil remedy with respect to Sections 2A:102-10 and 2A:102-11 would not be judicial interpre-

tation, it would be judicial legislation which should be exclusively limited to enactments by the New Jersey State Legislature.

POINT IV

A bankruptcy court is without power to grant compensation not expressly provided for by the Bankruptcy Act.

Although the Court of Appeals directed attorneys' fees be paid to the respondent's counsel as determined by the District Court, and that such fees be paid from the trust funds in question, the petitioner deems such a direction to be contrary to established bankruptcy practice.

A bankruptcy court has only such jurisdiction as is conferred upon it by the statute. *New Lamp Chimney Co.* v. *Ansonia B.C. Co.*, 91 U. S. 656, 23 L. Ed. 336. *Bardes* v. *Hawarden Bank*, 178 U. S. 524, 20 S. Ct. 1000, 44 L. Ed. 1175. *Taubel-Scott-Kitzmiller Co.* v. *Fox*, 264 U. S. 426, 44 S. Ct. 396, 68 L. Ed. 770. *Matter of Hollins*, 2 Cir., 229 Fed. 349, cert. den. 241 U. S. 661, 36 S. Ct. 448, 60 L. Ed. 1226. *Silberberg* v. *Ray Chain Stores, Inc.*, 3 Cir. 58 F. 2d 766, cert. den. *Winne* v. *Silberberg*, 287 U. S. 631, 53 S. Ct. 83, 77 L. Ed. 547. *Wheeling Structural Steel Co.* v. *Moss*, 4 Cir., 62 F. 2d 37; *Naylor* v. *Cantley*, 8 Cir., 96 F. 2d 761; *Moore* v. *Scott*, 9 Cir., 55 F. 2d 863. Although jurisdiction in bankruptcy is conferred on the district court, the latter when sitting as a Court of Bankruptcy is regarded as a separate court exercising powers and a jurisdiction distinct from its powers as a district court. *Hanna* v. *Brictson Mfg. Co.*, 8 Cir., 62 F. 2d 139. *Norris'* Case (D.C. Mich.) 18 Fed. Cas. 317, Fed. Cas. No. 10304.

It is unquestioned that bankruptcy courts have equity powers, but it is settled that the equitable powers may be exercised only within the limits of the Bankruptcy Act and subject to and consistent with the specific provisions contained therein. *Securities & Exchange Commission* v. *United States Realty & Improvement Co.*, 310 U. S. 434, 60 S. Ct. 1044, 84 L. Ed. 1293, *Young* v. *Higbee Co.*, 324 U. S. 204, 65 S. Ct. 594, 89 L. Ed. 890. *Matter of Columbia Ribbon Co.*, 3 Cir. 117 F. 2d 999, *Wheeling Valley Coal Corp.* v. *Mead*, 4 Cir. 171 F. 2d 916; *Burton Coal Co.* v. *Franklin Coal Co.*, 8 Cir., 67 F. 2d 796. In *Matter of Judith Gap Commercial Co.*, 9 Cir., 5 F. 2d 307, 309, the Court held that though bankruptcy proceedings are equitable in their nature "nevertheless they are to be administered in accord with the Bankruptcy Act and general orders, and not by virtue of any broad unlimited equity power".

Compensation for services rendered is but one of many phases of bankruptcy proceedings expressly governed by the Bankruptcy Act. The Courts of Appeal have uniformly held that the bankruptcy court lacks power to grant, and the policy of the Act is against compensation not expressly provided for by the Act. *Lane* v. *Haytian Corp.*, 2 Cir., 117 F. 2d 216, cert. den. 313 U. S. 580, 76 S. Ct. 1101, 85 L. Ed. 1537; *Guerin* v. *Weil, Gotschal & Manges*, 2 Cir. 205 F. 2d 302, *Berry* v. *Root*, 5 Cir., 148 F. 2d 945, cert. den. 326 U. S. 755, 66 S. Ct. 91, 90 L. Ed. 453. *In re First Bond & Mortgage Co.*, 5 Cir., 74 F. 2d 930, *Matter of Joslyn*, 7 Cir., 224 F. 2d 223, *Levin* v. *Barker*, 8 Cir., 122 F. 2d 969. In *Berry* v. *Root* (*supra*), 148 F. 2d 945, 946, the Court after noting that a bankruptcy court often applies equitable principles but "is not strictly a Court of Equity, but a statutory Court

created by the Bankruptcy Act, and governed by it", stated:

> "As to that proceeding the Act of 1898 has not adopted the equity precedents and practices as to costs, including costs as between attorney and client, commonly called an allowance of attorney's fees. The original Act and all the amendments and expansions have dealt specifically with the costs and attorney's and other fees to be allowed, and have dealt jealously with them. The fees allowable for services in each kind of bankruptcy proceedings have been provided, expressly or by implication, others are excluded."

CONCLUSION

It is respectfully submitted that the petitioner has shown that important questions exist for the granting of the petition for writ of certiorari and the writ should issue.

Respectfully submitted,

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APPENDIX

Judgment of the United States Court of Appeals

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty-first day of May one thousand nine hundred and sixty-five.

Present: HON. J. EDWARD LUMBARD,
Chief Judge,
Present: HON. THOMAS W. SWAN,
Present: HON. IRVING R. KAUFMAN,
Circuit Judges.

In the Matter
of

J. E. SCHECTER CORPORATION,
Debtor-Appellant,

CARRIER CORPORATION, AMERICAN RADIATOR and STANDARD SANITARY CORPORATION, SARCO COMPANY, INC., and SARCOTHERM CONTROLS, INC.,
Petitioners-Appellants.

Appeal from the United States District Court for the Eastern District of New York.

Judgment of the United States Court of Appeals

This cause came on to be heard on the transcript of record from the United States District Court for the Eastern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is reversed and that the action be and it hereby is remanded to said District Court for further proceedings in accordance with the opinion of this court with costs to the petitioners-appellants.

It is further ordered, adjudged and decreed that the appeal of the debtor be and it hereby is dismissed.

A. DANIEL FUSARO
Clerk

Opinion of the United States Court of Appeals

SWAN, *Circuit Judge*:

The legal issue presented by this appeal is whether certain funds held in a special account in a New York bank by J. E. Schecter Corporation, hereafter referred to as Schecter or the debtor, are trust funds. These funds were acquied as a result of the improvement of real property owned by Princeton University, located in Princeton, New Jersey, and called the "Engineering Quadrangle." The facts are stated in detail in the opinion of Judge Rayfiel and need not be here repeated except so far as necessary to supply a frame for subsequent discussion of the legal questions involved.

William L. Crow Construction Company, a New York Corporation, hereafter called Crow, was the general contractor for the Engineering Quadrangle. In January 1961 Crow entered into a subcontract with Schecter to provide all labor and materials for the satisfactory completion of the plumbing, heating, ventilating, and air conditioning work. Thereafter on November 27, 1962 Schecter filed a petition under Chapter XI of the Bankruptcy Act and an order was entered authorizing it to continue in possession of its assets, to continue its business under the supervision of the court, staying all creditors from proceeding with their claims, and referring the case to Referee in Bankruptcy William J. Rudin. In December 1963 the four appellants, on behalf of themselves and other contractors and materialmen similarly situated who had worked for or supplied goods to Schecter in connection with the Princeton project, petitioned the Referee to impress a trust on funds in possession of the debtor acquired as a result of the improvement of Princeton's Engineering Quadrangle. The Referee denied the petition. On No-

vember 17, 1964, the Referee's order was affirmed by Judge Rayfiel, with a remand of the matter to the Referee for the purpose of directing the debtor to take appropriate action to recover funds previously paid to certain claimants. This is the order before us on appeal.

For reasons hereafter stated we hold that the court erred in failing to impress a trust on the funds in question, and we dismiss the debtor's cross-appeal.

1. The cross-appeal of the debtor

The debtor has appealed the order of November 17, 1964 which remands the matter to the Referee in Bankruptcy for the purpose of directing the debtor to proceed with an appropriate motion to recover funds paid to six creditors. This part of the order was premised on the court's finding that no trust exists. Although we see no basis for an appeal by Schecter from the remand order, since it does not adversely affect the debtor but only the six creditors, see *Universal Oil Products Co.* v. *Cosden Petroleum Corp.*, 5 Cir., 178 F. 2d 495, we need not rest on that ground for the cross-appeal is mooted in any event by our holding that a trust should have been impressed. Accordingly, the cross-appeal is dismissed.

2. Applicability of the New York Lien Law

The subcontract between Crow and Schecter provided that "All matters relating to the validity, performance, interpretation or construction of the agreement or the breach thereof shall be governed by the Law of the State of New York." In reliance on this provision appellants contend that the New York Trust Fund Lien Law should be applied. See *Aquilino* v. *U. S. A.*, 10 N. Y. 2d 271, 275-

276. But even if we follow the directive of the choice-of-law provision, the claimants run into the barrier of the authoritative determination, by the highest state court, that the New York Lien Law does not apply to improvements to real property located outside the State of New York. *Allied Thermal Corp.* v. *James Talcott, Inc.*, 3 N. Y. 302, 165 N. Y. S. 2d 91 (1957). We hesitate to permit the contractual provision to overrule the considerations which compelled that decision, especially since—as we shall now explain—the claimants will be entitled to relief via the application of New Jersey law.

3. The New Jersey statutes

Section 2A:102-11 is printed in the margin.[1] It consists of two sentences. The first sets forth that moneys received by a subcontractor from the owner of real estate or from a contractor for the purpose of having a building erected are trust funds. The second declares that any subcontractor who pays or consents to the payment of

---

1. "Misappropriation of Funds Paid to Subcontractor for Building Purposes.

All monies received by a subcontractor from the owner or mortgagee of real estate, or any leasehold or other interest therein, or from a contractor, for the purpose of having a building erected, constructed, completed, altered, repaired or added to, are trust funds in the hands of the subcontractor to be applied to the amount of all claims due or to become due and owing from the subcontractor to all persons furnishing labor or materials to him for the erection, construction or completion of the building, or any alteration, repair or addition thereto, and any other reasonable and necessary charge in connection therewith. Any subcontractor or any officer, director or agent of the subcontractor, who pays or consents to the appropriation of such funds for any other purpose prior to the payment of all claims and charges for the payment of which the funds constitute a trust fund, is guilty of a misdemeanor. As amended L. 1954, c. 123, p. 599, §2."

such funds for any other purpose is guilty of a misdemeanor. *A priori* one would suppose that the first sentence is intended to give the beneficiaries of such "trust funds" a civil remedy. But no case has so held and under the New Jersey Constitution the title of a statute limits the scope of the enacting clauses; hence a construction which would give the statute a direct effect beyond the object expressed in the title must be rejected. Se *Jordan* v. *Moor*, 82 N. J. L. 552; *St. John, etc. Church* v. *Gengor*, 121 N. J. Eq. 349. The statute we are considering was originally entitled "A Supplement to an act entitled 'An act for the punishment of crime.'" See *Samuel D. Wasserman, Inc.* v. *Klahre*, 24 N. J. Super 143, 93 A. 2d 638. *Plevy* v. *Schaedel*, 44 N. J. Super 450, 130 A. 2d 910, but the title now reads "Misappropriation of Funds Paid to Subcontractor for Building Purposes." Whether this change of title is sufficient to permit the granting of a civil remedy we need not determine in view of the grounds upon which we predicate the existence of a trust.

4. Equitable principles are applicable.

It is elementary that a court of bankruptcy is also a court of equity. Under the undisputed facts we believe that the funds in question should be impressed with a trust on principles of equity and justice. Here the statute creates the trust, detailing its terms, and general equity principles may be employed to enforce it. See *Hiller & Skogland, Inc.* v. *Atlantic Creosoting Co.*, 40 N. J. 6,—n. 3, 190 A. 2d 380, 388 n. 3 (1963), citing with approval *Samuel D. Wasserman, Inc.* v. *Klahre, supra,* where the Superior Court, Appellate Division, although refusing to impose a constructive trust on funds in the hands of a third party not mentioned in the statute who lacked notice

of the trust fund character of the moneys, noted nevertheless that if there had been a statutory violation, the claimant "would have had whatever civil remedy might be appropriate to the circumstances under the general principles of law and equity." 24 N. J. Super at ——, 93 A. 2d at 631. Moreover, several New Jersey cases have held that where a fund is created for a special purpose, even though it does not meet the exact terms of the statutory trust, a trust will be imposed upon general equity principles. See *National Surety Corp.* v. *Barth*, 11 N. J. 506 (1953); *Morris Picker* v. *City of Bayonne, et al.*, 60 N. J. Super 251; *Wilson* v. *Robert A. Stretch, Inc.*, 44 N. J. Super 52, 58; *Stulz-Sickles Co.* v. *Fiedburn Constr. Corp.*, 114 N. J. Eq. 475. See also *Filardo* v. *Foley Bros.*, 297 N. Y. 217, cert. den. 336 U. S. 281; *Wickes Boiler Co.* v. *Godfrey-Keeler, Inc.*, 2 Cir., 116 F. 2d 842, modified 121 F. 2d 415, cert. den. 314 U. S. 686. Since Schecter was merely a conduit between the general contractor and the claimants, we see no reason for not applying those principles to this case. Indeed, if Schecter is permitted to remove the funds to New York and allocate them in this manner, it can misappropriate sums derived from a real estate improvement in New Jersey with complete immunity, thereby thwarting the New Jersey criminal statutes and also avoiding any quasi-fiduciary obligations.

For the foregoing reasons we hold that the court erred in failing to impress a trust on the funds in question, and we direct that attorney's fees as determined by the District Court, be paid from the trust funds.

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Supreme Court of the United States

OCTOBER TERM, 1965

No. 463

IN THE MATTER
of
J. E. SCHECTER CORPORATION,
Petitioner,
and
CARRIER CORPORATION, AMERICAN RADIATOR & STANDARD SANITARY CORPORATION, SARCO COMPANY, INC. and SARCOTHERM CONTROLS, INC.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

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Supreme Court of the United States

OCTOBER TERM, 1965

No. 463

IN THE MATTER

of

J. E. SCHECTER CORPORATION,

Petitioner,

and

CARRIER CORPORATION, AMERICAN RADIATOR & STANDARD SANITARY CORPORATION, SARCO COMPANY, INC. and SARCOTHERM CONTROLS, INC.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

Opinions Below

The opinion and order of the Referee in Bankruptcy appear in the Appendix at pages 31a through 39a. The opinion of the United States District Court for the Eastern District of New York which upheld the decision of the Referee in part, but remanded the matter to him for further proceedings, is reported at 234 F. Supp. 474. The opinion of the Court of Appeals for the Second Circuit, which reversed the decision of the District Court and dis-

missed the cross-appeal of the petitioner, is reported at 347 F. 2d 153 and also appears with the judgment of the Court of Appeals at pages 28 through 34 of the petition.

Jurisdiction

The judgment of the Court of Appeals was entered on May 21, 1965. The petition for certiorari was filed on August 17, 1965. Jurisdiction of this Court is invoked under 28 U. S. C. § 1254 (1) and Section 24c of the Bankruptcy Act, 11 U. S. C. § 47c.

Statutes Involved

Respondents find no fault with the citation by petitioner of the relevant New Jersey statutes, except that the captions are not completely accurate. Title 2A of the New Jersey statutes is captioned: "Administration of Civil and Criminal Justice." Subtitle 6 thereunder is captioned "Specific Civil Actions," and Subtitle 10 is captioned "Crimes." Lest undue emphasis be placed on captions and cross-references, the Court's attention is directed to the Preamble to Title 2A, paragraph 7 which provides:

> "The classification and arrangement of the several sections of said Title 2A have been made for the purpose of convenience, reference and orderly arrangement, and therefore no implication or presumption of a legislative construction is to be drawn therefrom."

and to paragraph 8 which states:

> "In the construction of the said Title 2A . . . no outline or analysis of the contents of said title or of any subtitle . . . no cross-reference or cross-reference note and no headnote or source note to any section of the said Title 2A shall be deemed to be a part of the said Title."

On the trust fund issue, no federal statute is involved, the Bankruptcy Court merely being the forum for determining rights to a fund in the Court's actual or constructive possession. It is undisputed that local law is crucial on that issue.

The Bankruptcy Act is involved only by petitioner's "Argument" on counsel fees, but not by mention in "Questions Presented For Review" or the "Statement of the Case". Petitioner contends that the Bankruptcy Act makes no provision for counsel fees in this case. Respondents contend that insofar as the Bankruptcy Act vests the Bankruptcy Court with equity powers, such power includes the traditional power to allow counsel fees when a fund is created for the benefit of others.

Chapter 2 of the Bankruptcy Act (11 U. S. C. § 11) provides:

> "CREATION OF COURTS OF BANKRUPTCY AND THEIR JURISDICTION. (a) The Courts of . . . bankruptcy . . . are hereby invested . . . with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this act . . ."

The New York Lien Law, Section 70 *et seq.* was involved in the courts below and appears in part in the appendix (9a), but for present purposes need not be repeated here.

Questions Presented for Review

Should this Court exercise its sound judicial discretion and grant certiorari when:

(a) The Court of Appeals has not decided an important New Jersey question in conflict with applicable New Jersey law, but in fact is entirely in accord with it; and when

(b) No federal issue is involved, although petitioner raises the *Erie* v. *Tompkins* doctrine so as to fall within this

Court's appellate jurisdiction, notwithstanding that the Court of Appeals clearly applied local law; and when

(c) The Court of Appeals left unanswered alternative grounds for relief under New York and New Jersey statutes by granting relief under New Jersey decisional law and New Jersey as well as general principles of equity and justice; and when

(d) The petitioner, on the question of counsel fees payable out of the fund, is not an aggrieved party and therefore has no standing to appeal, and when, in any event, the decision of the Court of Appeals on the issue of compensation is in harmony with decisions of this Court and the New Jersey courts, and not in conflict with any cited by the petitioner.

Statement of the Case

The facts appear in the opinion of the District Court in detail and in the opinion of the Court of Appeals to the extent necessary to frame the legal questions involved. Respondents cannot concur with petitioner's presentation of the case.

In January, 1961, William L. Crow Construction Company, a New York corporation, hereafter called Crow, general contractor in the improvement of real property owned by Princeton University, located in Princeton, New Jersey, and known as the "Engineering Quadrangle", entered into a subcontract with the petitioner, J. E. Schecter Corporation, hereafter called Schecter or the debtor, to provide all labor and materials for the plumbing, heating and air-conditioning work. The sub-contract provided that "All matters relating to the validity, performance, interpretation or construction of the agreement or the breach thereof shall be governed by the Law of the State of New York" (13a).

In September, 1962, Schecter wrote to Crow, setting forth the names of forty-one subcontractors and materialmen who had performed work for and/or supplied materials to Schecter for the Princeton job, and to whom Schecter was indebted, and requested Crow to pay the said claimants from the balance due Schecter a sum on account equal to 50% of the respective claims, but said sums were never paid (16a).

On November 27, 1962, Schecter filed a petition under Chapter XI of the Bankruptcy Act and an order was entered authorizing it to continue in possession of its assets, to continue in business, staying all creditors from proceeding with their claims, and referring the case to Referee in Bankruptcy, William J. Rudin.

In July, 1963, one of the unpaid subcontractors, Johnson Service Company, moved before the Referee for an order permitting it to prosecute an action against the debtor on behalf of itself and others similarly situated for an accounting of the trust funds derived from the Princeton project, but Johnson did not proceed further with the motion (27a-30a). Instead, Schecter filed a petition for an order compromising Schecter's claim against Crow for $165,000, compromising the claims of six creditors, including Johnson Service Company, against the fund for approximately 30% of their claims, with no mention of the fact that there were thirty-five other claimants and providing that the balance be paid to Schecter and deposited in a depositary designated by the Court (13a). The order was signed by Referee Rudin (11a), and the terms were thereupon carried out, with a balance of $92,816.67 being paid over to Schecter and being held in a special account in the debtor's name. No notice of this proceeding was given to the thirty-five other creditors of the debtor remaining from the Princeton job.

In December, 1963, the four respondents, on behalf of themselves and others similarly situated, petitioned the

Referee to impress a trust under the laws of New Jersey and New York on said funds in the debtor's possession and for legal fees to be paid out of said trust fund (2a-18a).

The Referee denied the petition and Judge Rayfiel upheld him on the grounds that no trust could be impressed under New York law since its Lien Law only applied to an improvement of real property located in the State of New York and that the intent of Crow and Schecter to have New York law apply must bow to the more significant contacts in New Jersey, and that the New Jersey statute was criminal in scope and provided no civil remedy for a "diversion" of funds received by a contractor for a New Jersey improvement. The District Court, however, remanded the matter to the Referee for the purpose of directing the debtor to proceed with an appropriate motion to recover the funds paid to the six creditors (47a).

The Court of Appeals reversed the District Court and impressed a trust on the funds in the debtor's possession derived from the Princeton project on equitable principles as enunciated in New Jersey cases, and allowed counsel fees out of said fund, remanding the matter to the District Court for further proceedings in accordance with the opinion. The Court of Appeals also denied the cross-appeal of the petitioner for the reason that the return of the monies paid to six creditors was mooted by the impressing of a trust.

After remand, respondents obtained an order signed by Referee Rudin dated July 29, 1965, a copy of which is set forth in the Appendix (24), which details the steps to be taken in order to implement the decision of the Court of Appeals.

The Court of Appeals, in respondents' view, did not definitely rule out the applicability of New York law or a remedy based solely on the New Jersey statute, but found it unnecessary to determine those questions as it impressed a trust on other grounds. While respondents rely primarily

on New Jersey law inasmuch as the improvement was located in New Jersey, they take the position that if the New Jersey statutory or decisional laws do not afford relief, respondents can look to New York law alternatively as a third-party beneficiary of the contractual provision which sought to apply New York law.

Respondents do not seek an allowance for counsel fees over and beyond the amounts due the unpaid claimants, but only seek it from those participants in the trust fund to be paid out of their recovery. Respondents fail to see how petitioner is affected by this part of the Court of Appeals' decision. In any event, the only question would be the power of the bankruptcy court to allow counsel fees in this type of case, and this Court has already passed affirmatively on that issue, and the cases cited by the petitioner are not in conflict with the decisions of this Court or the decision of the Court of Appeals.

Upon the undisputed facts and the applicable New Jersey law, the decision of the Court below was absolutely correct.

ARGUMENT

I

There is no basis for granting certiorari.

A. Solely State-created rights are involved and *Erie* v. *Tompkins* has no applicability.

The existence of a trust fund is strictly a question of local law and both petitioner and respondents have adopted this view. The subsidiary question of which local law to apply is not before this Court, as the Court of Appeals granted relief under New Jersey law, the choice of the petitioner and accepted by respondents as their primary basis for relief. The only question, therefore, insofar as *Erie* v. *Tompkins* (304 U. S. 64, 58 S. Ct. 817, 82 L. Ed.

1188), is concerned, is whether the Court of Appeals applied local law, and not whether they applied it correctly;

The opinion of the Court of Appeals could not be any plainer. It relied mainly on the following for its decision: (1) An expression by the highest court of New Jersey in the recent case of *Hiller & Skogland, Inc.* v. *Atlantic Creosoting Co., Inc.*, 40 N. J. 6, 20 n. 3, 190 A. 2d 380, 388, n. 3 (1963) citing with approval a decision of the Superior Court, Appellate Division of the State of New Jersey, *Samuel D. Wasserman, Inc.* v. *Klahre*, 24 N. J. Super. 143, 93 A. 2d 638, which said that if there were a violation of the private improvement statute, the Court would give "whatever civil remedy might be appropriate to the circumstances under the general principles of law and equity". (2) Holdings in several New Jersey cases wherein trusts were impressed, not directly under the statutes there involved, but under general equitable principles. *National Surety Corp.* v. *Barth*, 11 N. J. 506 (1953) and other cases cited in the opinion.

The Court of Appeals also cited a federal case in New York involving a similar statute, former Section 36a of the New York Lien Law, which was deemed to be a criminal statute, but where the Court nevertheless impressed a trust. *Wickes Boiler Co. Inc.* v. *Godfrey-Keeler, Inc.*, 2 Cir., 116 F. 2d 842, mod. 121 F. 2d 415, cert. den. 314 U. S. 686, and another case of far-reaching importance, *Filardo* v. *Foley Bros. Inc.*, 297 N. Y. 217, cert. den. 336 U. S. 281 (1948), where the New York Court of Appeals said:

> "With the beneficial results of the statute so mainfest, if plaintiff may not sue to enforce it, the benefits accorded would indeed be empty and illusory. He would find himself in the position of having been given a benefit he is unable to enjoy, a right he is helpless to enforce."

The petitioner, on the other hand, does not even mention or cite the *Hiller & Skogland* case, *supra,* which is rather astonishing when considered in the light of its contention that the Court of Appeals did not apply New Jersey law. The petitioner also makes no attempt to explain the vitally important statement made by the Appellate Court in the *Wasserman* case, as quoted in the Court of Appeals' opinion—which is the crux of this case. Thus, the petitioner has ignored the very same criteria set forth in a case it cited on pages 10-11 of its petition, *Yoder et al.* v. *Nu-Enamel Corporation,* 8 Cir., 117 F. 2d 488.

The Court of Appeals decided that New Jersey law applied and granted relief unanimously on equitable principles as enunciated by the authoritative New Jersey cases cited in its opinion, and certiorari on the grounds that *Erie* v. *Tompkins* has been ignored, should therefore be denied.

B. There are no matters of federal importance to be considered.

There is no conflict among the circuits on the issue presented, and no cases are cited in the petition to demonstrate any conflict. There is no important question of federal law which has not been, or should be settled by this Court. No issue touching the federal interest is presented. The issue is narrow and not likely to recur. The trust fund issue is strictly a matter of local law. See *Collier* on Bankruptcy, Volume 4, pages 1210-1211.

As to the power of the bankruptcy court to award counsel fees out of the fund, this matter had long ago been settled by this Court in *Trustees* v. *Greenough,* 105 U. S. 527, 533, when this Court said:

> "The rule that a party who recovers a fund for the common benefit of creditors is entitled to have his costs and expenses paid out of the fund, prevails in bankruptcy cases."

And in *Sprague* v. *Ticonic Bank*, 307 U. S. 161, 167, this Court said:

> "In any event such allowances are appropriate only in exceptional cases and for dominating reasons of justice. But here we are concerned solely with the power to entertain such a petition."

New Jersey has also accepted the doctrine of *Trustees* v. *Greenough, supra*. See *Babbitt* v. *Fidelity Trust Co.*, 72 N. J. Eq. 745, 66 A. 1076.

Any limitations that may exist on the power of the bankruptcy court to allow counsel fees are those imposed in the bankruptcy itself, and not in any controversy in equity arising out of the bankruptcy in which the bankruptcy court will follow the precedents and practice of a court of equity and allow counsel fees, referred to traditionally as costs as between solicitor and client. Even the case of *Berry* v. *Root*, 5 Cir., 148 F. 2d 945, cert. den. 326 U. S. 755, and others cited by petitioner, and which did not involve a fund before the Court, acknowledged the power to allow counsel fees under circumstances present in this case. The only reservation sometimes placed is the requirement that the benefits be accepted by the beneficiaries. However, as demonstrated heretofore, steps are under way (24) to give the other beneficiaries an opportunity to share in the fund and to accept the benefits.

In any event, the petition should not be granted solely on the question of counsel fees for the further reason that petitioner is not an aggrieved party and therefore has no standing to review the decision allowing it? Respondents do not seek any sum over and beyond the amount due the unpaid claimants for counsel fees, but merely an allowance out of the sums being paid to each creditor, so that the creditors who did not participate in this litigation are not unjustly enriched at the expense of the four claimants and their attorneys who instituted the proceeding before the

Referee, petitioned the District Court for review and then appealed to and obtained a reversal from the Court of Appeals and are now opposing certiorari before this Court. In fairness and in equity, the expenses and legal fees as determined by the District Court should be shared ratably out of the fund. The petitioner will be unaffected by this relief. The only ones affected by any allowance of counsel fees would be the thirty-five other participants in the fund against which the fees would be chargeable.

It is well-settled that an appellant cannot be heard to complain of an error which does not harm him. He must be aggrieved by the judgment or decree for which the relief is sought. It must prejudice him in his rights or adversely affect his legal interests, otherwise, he is not entitled to appeal therefrom. *Public Service Commission* v. *Brashear Freight Lines, Inc.*, 306 U. S. 204, 83 L. Ed. 608, rearg. den., 306 U. S. 669, 83 L. Ed. 1063; *Kirkpatrick* v. *Eastern Milling & Export Co.*, 135 F. 151; *Marceau* v. *Great Lakes Transit Corp.*, 2 Cir., 146 F. 2d 416; *Highway Construction Co. of Ohio* v. *City of Miami, Fla.*, 5 Cir., 126 F. 2d 777; Cyclopedia of Federal Procedure, Volume 14, 67.05, page 121.

The Court of Appeals did not decide any federal question in a way to conflict with applicable decisions of this Court, nor did it conflict with any guaranty of basic fairness secured by the Constitution or implied in the nation's laws so as to call for the exercise of this Court's power of supervision. In fact, the decision of the Court of Appeals is in furtherance of this Court's doctrines. See: *Aquilino* v. *United States of America, et al.*, 363 U. S. 509, 80 S. Ct. 1277; *Pearlman* v. *Reliance Insurance Company*, 371 U. S. 132, 135. In the latter case, this Court said:

> "Property interests in a fund not owned by a bankrupt at the time of the adjudication, whether complete or partial, legal or equitable, mortgages, liens, or simple priority of rights, are of course not a part of the

bankrupt's property and do not vest in the trustee. The Bankruptcy Act simply does not authorize a trustee to distribute other people's property among a bankrupt's creditors. So here if the surety at the time of adjudication was, as it claimed, either the outright legal or equitable owner of this fund, or had an equitable lien or prior right to it, this property interest of the surety never became a part of the bankrupt estate to be administered, liquidated and distributed to general creditors of the bankrupt."

Moreover, the Court of Appeals made it clear that the consequence of its decision would be to guarantee basic fairness and to bring about the fulfillment of the New Jersey legislative intent that funds from a real property improvement went to those who contributed to the improvement.

II

The decision below is clearly correct.

While the Supreme Court of New Jersey in *State* v. *Low*, 18 N. J. 179 (1955), and the clear language of Section 2A:102-11 of the New Jersey statutes describe the monies received as "trust funds", the New Jersey courts have not ruled squarely on the issue presented herein, i.e., whether a bankruptcy court could impress a trust under New Jersey law in favor of job claimants on funds in the possession of a debtor derived from a New Jersey improvement.

However, as noted before, clear expressions by the highest and next highest courts of the State indicate that civil relief would be afforded and formed the main basis for the decision of the Court of Appeals.

It should be noted that nothing more is sought herein than the precise application of the statute in favor of

the statutory beneficiaries and against the statutory trustee, without any complicated issue of tracing the *res*, creation of a constructive trust against funds in the hands of third parties, or the imposition of a civil remedy against someone other than the trustee.

The petitioner relies heavily on a lower court New Jersey case, *Plevy* v. *Schaedel*, 44 N. J. Super. 450, 130 A. 2d 910 (Superior Court, Law Division, 1957), and the statutory interpretation of the court in contrasting the legislative treatment given by the State of New Jersey to public improvements as against private improvements.

Respondents contend this reliance is unwarranted for the following reasons:

(1) The *Plevy* case is clearly distinguishable from our case in that *Plevy* involved a suit against officers of the corporate debtor-trustee for a diversion and not one against the statutory trustee for an accounting; (2) The Supreme Court of New Jersey, in its footnote reference to the private improvement statute in the *Hiller & Skogland* v. *Atlantic Creosoting Co. Inc.* case, *supra*, cited the case of *Samuel D. Wasserman Inc.* v. *Klahre, supra*, as allowing civil liability under the statute, but did not cite *Plevy*, the only other decision interpreting the statute and more recent in time than *Wasserman*; (3) In the same footnote reference, the court noted that a different legislator introduced the private improvement statute than the one who introduced the public improvement statute; and (4) A closer look at the public and private improvement statutes demonstrates that the differences in substance are nil, and they were treated differently only because of a different approach by the two legislators introducing the respective bills.

Respondents contend that the statements in the *Hiller & Skogland* and *Wasserman* cases, constitute clearcut support for its view that civil remedies are available under the New Jersey statute. Further statements in the *Hiller*

& Skogland opinion lend strength to this conviction and demonstrate that as between the parties, the beneficiaries must prevail. With respect to the trust fund statute on a public job, which should apply equally to a private improvement, the Supreme Court of New Jersey said:

> "While it cannot be said that the trust fund prescribes a full-blown trust relationship all the way down the ladder with consequent effect upon strangers to the construction project, the underlying thought is clear that all those directly involved should do the right and honorable thing . . ."

and later, the Court said:

> "A court should not hesitate to translate that legislative conception into a positive duty and to compel the appropriate use of payments where the payee knows their source and obviously intended purpose . . . for a court to do less would be to sanction sharp practice—indeed immoral conduct—in the business community. That day should have long since passed as far as the judiciary is concerned."

Its endorsement of the *Wasserman* case, its failure to cite *Plevy* v. *Schaedel,* its mention that different legislators introduced the public improvement and private improvement statutes, coupled with the sweeping language of its decision insofar as the public improvement statute was concerned, make it evident that the Supreme Court of New Jersey would sanction the relief granted by the Court of Appeals.

The court in the *Plevy* case cited two cases in support of its decision, the *Wasserman* case, *supra*, and *Raymond Concrete Pile Co.* v. *Federation Bank & Trust Co.*, 288 N. Y. 452, 45 N. E. 2d 486, affd. on reargument, 290 N. Y. 811, 48 N. E. 2d 709. These cases likewise are distinguishable in that both involved efforts to impose constructive trusts on funds in the hands of third parties not mentioned in the

statute who lacked notice of the trust fund character of the monies. In neither case was relief sought directly against the statutory trustee.

In the *Wasserman* case, a job claimant who had accepted checks from the debtor in release of a mechanic's lien sought to recover monies collected by another creditor on a sheriff's execution against the debtor's bank account. The court refused to impress a trust against the execution creditor on the ground that such action was not authorized by the statute.

However, in rejecting the trust beneficiary's claim, the court nevertheless enunciated principles which support the relief sought herein, to wit, that criminal statutes do have incidental effects and civil remedies arising therefrom. The following are excerpts from the opinion:

> "We are satisfied that had Candrille violated the statute, the plaintiffs would have had whatever *civil remedy might be appropriate to the circumstances under the general principles of law and equity* but Candrille did not violate the statute; the sheriff levied on the fund without leave of Candrille . . .
>
> "The mingling of the fund with other monies in Candrille's general bank account did not destroy plaintiff's *interest in the funds* . . .
>
> "The interest that plaintiff actually had in the account was at most an undisclosed equitable lien . . .
>
> "In New Jersey, there is no clear rule on the subject . . . We think that in each case the facts must be analyzed to determine on broad principles whether the judgment creditor or the lienor has the stronger claim . . ." (Emphasis added.)

A careful reading of the *Wasserman* case indicates (1) that job claimants embraced within the statutory protection have an interest in the fund as trust beneficiaries and (2)

that under certain circumstances, including, but surely not limited to a violation of the statute by the trustee, civil remedies would be available (other than for goods sold and delivered). An accounting by the trustee, either in a bankruptcy, insolvency or estate proceeding, should likewise be available as a logical outgrowth of the *Wasserman* decision.

It should be noted that in neither the *Plevy, Wasserman* nor *Raymond Concrete* cases did the courts sanction a misappropriation of the debtor's trust funds by the debtor itself.

A comparison of the public and private improvements does not lead to any contrary result.

In the early part of 1932, three statutes were passed, dealing with mortgagors, general contractors and sub-contractors respectively on private improvements, and with changes not relevant herein, these laws are in effect today as Sections 2A:102-9, 2A:102-10 and 2A:102-11. Later in 1932, a different legislator introduced two other separate statutes dealing with public improvements, and which are now embodied in Sections 2A:44-148 and 2A:102-12.

Section 2A:102-11, the private improvement statute we are dealing with, provides as follows:

> "All monies received by a subcontractor . . . from a contractor, for the purpose of having a building erected . . . . *are trust funds in the hands of the subcontractor to be applied to the amount of all claims due or to become due and owing from the subcontractor to all persons furnishing . . . materials* to him. . . . Any subcontractor or any officer, director or agent of the subcontractor, who pays or consents to the appropriation of such funds for any other purpose prior to the payment of all claims and charges for the payment of which the funds constitute a trust fund, is guilty of a misdemeanor." (Emphasis added.)

It should be noted that this section consists of two sentences. The first sentence provides that all monies received by a subcontractor are *trust funds* in the hands of the subcontractor *to be applied to the amount of all claims due or to become due to materialmen and others.* The second sentence of the statute creates the criminal offense.

Section 2A:102-12, the public improvement statute, differs from the private improvement statute but these differences favor respondents' view herein. It provides as follows:

> "All monies paid by the state . . . to any person . . . for the making of any public improvement, *shall constitute a trust fund in the hands of such person as contractor.* Any such person who shall use any of the moneys so received for a purpose other than the payment of claims for labor or material . . . is guilty of a misdemeanor." (Emphasis added.)

Thus, this statute is also in two parts, but the first part ends with the establishment of the trust fund in the hands of the contractor and *does not contain any directions about its application nor does it name any beneficiaries.* The second sentence simply creates the criminal offense for misuse of the fund.

Section 2A:44-148, also dealing with public improvements, starts off by repeating substantially the same language as appears in the first part of 2A:102-12 (the criminal statute) but then continues with an application clause, as follows:

> "All monies paid by the State of New Jersey . . . shall constitute a trust fund in the hands of such person as such contractor *until all claims for labor, material . . . shall have been fully paid.*" (Emphasis added.)

It is apparent that the legislator, in the case of the public improvement statutes, wished to separate the civil from the criminal and accomplished that objective by handling the application of the trust funds in a separate statute. In the case of the private improvement statutes, the civil and criminal provisions were handled together and the first sentence of those statutes embodies all the elements of a trust, i.e., a trustee, a fund, directions as to its use and specified beneficiaries.

The public improvement criminal statute (2A:102-12) is obviously only criminal because the clause creating the trust ends without stating its purpose or providing for its application, and logically so, for the disposition of the trust fund is dealt with in 2A:44-148, where the legislator restated the creation of the trust but added the words "until all claims for labor, materials . . . shall have been fully paid". In contrast, substantially the same words were already contained in the private improvement statute, Section 2A:102-11 which provided that "All monies . . . are trust funds in the hands of a subcontractor to be applied to the amount of all claims . . . due . . . from the subcontractor to all persons furnishing . . . materials . . ."

Respondents therefore submit that a closer examination of the New Jersey statutes draws one to the conclusion that no inference can be drawn by any different legislative treatment, except an inference favorable to the respondents, to wit, that both groups of statutes created civil remedies, but in different ways, only because the legislator on the public improvement statute merely desired more clarity and an orderly separation of the civil from the criminal provisions.

If the law of New Jersey is to be determined by a choice between the lower court decision of *Plevy* or the Appellate Division decision of *Wasserman*, it is clear that *Wasserman*, especially in the light of its approval by the Supreme Court of New Jersey in the *Hiller & Skogland* case, is

a more authoritative exposition of New Jersey law than *Plevy*. And the *Wasserman* case clearly keeps the door open for civil remedies under the statute.

In any event, neither the *Wasserman* nor the *Plevy* case is clearcut authority for the factual situation involved herein—a conflict between job claimants on the one hand and the debtor and, indirectly, its unsecured creditors on the other hand. On this conflict, there are no New Jersey cases directly in point. It is submitted, therefore, that the Court of Appeals was free to determine what the highest court of the state would rule in a similar case.

The other case cited in the *Plevy* case, *Raymond Concrete Piling Co.* v. *Federation Bank & Trust Co., supra,* also involved rights of a third party under a comparable New York criminal statute, but the dicta in that case which seemed to deny a civil remedy was later disapproved by the New York Court of Appeals in the case of *Aquilino* v. *U. S. A.*, 10 N. Y. 2d 271, 276, when it said:

> ". . . This holding, distinguished from the dicta in that case, clearly supports the view that a 36-a contractor-trustee holds the funds he receives as trustee, rather than as owner, until he has paid the claims of all the statutory beneficiaries."

There are three cases in the federal courts which are squarely in point, and while they involve application of the law of New York, the statute then involved, Section 36-a of the Lien Law, was similar to the present New Jersey statute, i.e., it was on its face criminal in impact, and yet, the Federal Courts did not hesitate to impress a trust when the fund was in the possession of the bankrupt or debtor. *Albert Pick Co.* v. *Travis*, 6 F. Supp. 486 (E. D. N. Y. 1933); *In re Heintzelman Const. Co.*, 34 F. Supp. 109 (W. D. N. Y. 1940); *Wickes Boiler Co. Inc.* v. *Godfrey-Keeler, Inc.*, 2 Cir., 116 F. 2d 842, mod. 121 F. 2d 415, cert. den. 314 U. S. 686.

Section 36-a of the Lien Law of New York was captioned: *"Contractor who diverts funds guilty of larceny"*.

The Court, in *Albert Pick Co.* v. *Travis, supra,* held that the funds in the hands of the contractor were trust funds under the New York criminal statute and so aptly said:

> "The intention of the Legislature of the State of New York was to protect sub-contractors, materialmen and laborers-contractors cannot avoid their responsibilities by making preferential payments out of trust funds and then filing petitions in bankruptcy or having involuntary petitions filed against them. To follow the trustee's contention that the funds should be distributed among all the creditors would nullify the very purpose of the statute, which was to distribute the specific fund to a preferred class of creditors. There would be no purpose for the lien law were it not that the State intended to protect the very class that the statute outlined. If the contractor attempts to deprive the lienors of their rights, the court should restrain and not help facilitate the avoidance of lawful obligations."

The case of *Wickes Boiler Co., Inc.* v. *Godfrey Keeler, Inc., supra,* is even more authoritative because it involved an application to a Referee in a Chapter XI bankruptcy proceeding for an order similar to the one herein, except that the petitioners there sought to impress a trust on a receivable and not on monies in the debtor's bank account. The *Wickes Boiler* case dealt with the same criminal statute as in the *Albert Pick Co.* v. *Travis* case, and the debtor likewise sought to use the monies to consummate a settlement with its creditors. The Circuit Court of Appeals sustained the Referee in impressing a trust.

Several other related cases support the respondents' view. *Maull* v. *Stokes,* 31 Del. Ch. 188 (1949); *Estate of Liebman,* 189 Misc. 282, 60 N. Y. S. 2d 482; *In Re Korsder's Estate,* 168 Misc. 553, 6 N. Y. S. 2d 324.

In the *Plevy* case, the Court said that since the statute is a criminal one, it should be strictly construed. While this is a general rule of construction, it is also firmly established that where a statute is both remedial and penal, the remedial part will be liberally construed and the penal part strictly construed. Respondents are not attempting to penalize or imprison the debtor; they are only seeking to recover monies which the legislature intended them to receive. See *State* v. *Meinken*, 10 N. J. 348 (1952); *Filardo* v. *Foley Bros. Inc., supra.* Moreover, appellants contend that the statute is so clear that it calls for little or no construction as between the sub-contractor and the materialman.

The remedies cited by the petitioner as being available under the laws of New Jersey dealing with mechanic's liens and "stop notices" are only concerned with tying up monies in the hands of the owner of the real property improvement, whereas the trust fund statutes are designed to insure that monies in the hands of a contractor or sub-contractor are paid over to materialmen and other sub-contractors. And while the Appellate Court in the *Wasserman* case did mention the fact that a lien could have been filed in weighing the equities of the parties, the court there was not dealing with a controversy between the trustee and the beneficiaries, but between the beneficiaries and a third party, nor did the court in the *Wasserman* case hold that filing of a lien or "stop notice" was a condition precedent in order to receive "whatever civil remedy might be appropriate under the circumstances." Cf. *Wickes Boiler Co., Inc.* v. *Godfrey-Keeler, Inc., supra.*

A trust was properly impressed on equitable principles. It is elementary that a Court of bankruptcy is also a Court of equity, and in view of all the facts and circumstances in this matter, the Court of Appeals was correct in affording relief herein on general principles of equity and justice. *Clews* v. *Jamieson*, 182 U. S. 461 (1901); 1 *Pomeroy on Equity Jurisprudence*, Section 158.

The record reveals quite clearly that the petitioner made no excuse for its attempt to prefer a small group of job creditors to the exclusion of and without notice to thirty-five others. The circumstances show that the petitioner was aware of trust fund claims (16a). When its payments to the select few were revealed, it made an about-face and denied any trust fund obligations (17a).

If the petitioner is allowed to use trust funds in this manner, then surely it would be a simple matter for any contractor to misappropriate construction funds with complete immunity by merely receiving all funds on a New Jersey job in the State of New York. The contractor would thereby thwart the New Jersey criminal statute and be free of any trust fund obligations, or the contractor could simply hold the monies in a New Jersey bank account indefinitely, file a Chapter XI petition, with no consequences to it for not paying out to its job creditors.

Surely a Federal Court, under principles of equity, should not permit a debtor to violate the New Jersey statute and frustrate the intent of the New Jersey legislature. Such interpretation of the legislative intent should not be made by any court, no less a court of bankruptcy and equity.

The Court of Appeals also relied on numerous New Jersey cases which hold that where a fund is created for a special purpose even though it does not fall within the confines of the statutory trust, a trust will be impressed under general equity principles. *National Surety Corp.* v. *Barth*, 11 N. J. 506 (1953); *Morris Picker* v. *City of Bayonne, et al.*, 60 N. J. Super. 251; *Wilson* v. *Robert A. Stretch, Inc.*, 44 N. J. Super. 52, 58; *Stulz-Sickles Co.* v. *Fiedburn Const. Corp.*, 114 N. J. Eq. 475.

It would seem immaterial that the foregoing cases involved the public improvement statutes, and the Court of Appeals correctly used all the equitable principles at its command, such as not allowing a person to avoid

responsibility by violating a statute, estoppel, having equity to do what should be done, applying a fund for its intended use when the fund is under the control of a court and other principles of law and justice, in order to grant the relief prayed for herein. See *Filardo* v. *Foley Bros., supra.*

If the petitioner is to prevail in this case, would it not be tantamount to holding that the very ones whom the law was intended to protect were helpless to secure that protection, and, even in New Jersey, that the petitioner would be immune from criminal prosecution so long as it retained possession of the fund indefinitely, or, as in this case, received the funds outside of the State of New Jersey and would be free to divert same in or out of a bankruptcy Court? Respondents do not believe that this Court will countenance such a result, or that the case is the kind of case warranting the exercise of this Court's discretionary review.

Under the strict tests for discretionary review, there must be an actual conflict with applicable local law decisions. See Weiner, 68 Harvard Law Review 20, 61. Such conflict is not present in this case. To the contrary, the decision of the Court of Appeals is in accord with New Jersey law.

CONCLUSION

For the foregoing reasons it is respectfully submitted that this petition for a writ of certiorari should be denied.

Respectfully submitted,

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SCHWARTZ, WEISSBERGER, LEICHTER & STORCH,
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Of Counsel.

APPENDIX

UNITED STATES DISTRICT COURT,

EASTERN DISTRICT OF NEW YORK.

No. 62-B-934

In the Matter

—of—

J. E. SCHECTER CORPORATION,

Debtor.

ORDER

The petitioners Carrier Corporation, American Radiator & Standard Sanitary Corporation, Sarco Company, Inc. and Sarcotherm Controls, Inc. having appealed to the United States Circuit Court of Appeals for the Second Circuit from an order of the Hon. Leo J. Rayfiel, one of the Judges of this Court, entered in this proceeding on the 17th day of November, 1964, which denied a petition for review of an order of The Honorable William J. Rudin, Referee in Bankruptcy, dated the 20th day of July, 1964, to the extent that the petition sought to impress a trust on funds in the possession of the debtor, and to recover counsel fees out of said funds, but which granted the petition for review to the extent that the matter was remanded to the Referee for the purpose of directing the debtor to proceed with an appropriate motion to recover funds paid to six creditors pursuant to a prior order of the Referee dated July 23, 1963, and said Circuit Court of Appeals having issued its order dated the 21st day of May, 1965, and its mandate dated the 11th day of June, 1965 having been transmitted to and received by the Clerk of this Court

on the 14th day of June, 1965, wherein it was ordered, adjudged and decreed that such order of the District Court be reversed, with costs assessed at $282.66 in favor of petitioners-appellants, and that the matter be remanded to the District Court for further proceedings in accordance with the opinion of the Court wherein it was held that the District Court erred in not impressing a trust on the funds in question and directed that counsel fees be awarded out of said funds as determined by the District Court, and that the alternative relief of directing the recovery of funds paid to six other creditors was moot.

Now, upon the aforesaid order, mandate and opinion of the United States Circuit Court of Appeals for the Second Circuit, it is

ORDERED, ADJUDGED and DECREED that the sum of $92,316.87 and any additions or accretions thereto paid by William L. Crow Construction Company to the debtor on account of the real property improvement known as "Engineering Quadrangle" at Princeton University, Princeton, New Jersey, pursuant to the order of this Court dated July 23, 1963, constitute and are trust funds in the hands of said debtor to be applied first to the payment of unpaid claims of all persons furnishing labor and materials to J. E. Schecter Corporation for the erection, construction and completion of said improvement or any alteration, repair or addition thereto, and any other reasonable and necessary charges in connection therewith, and it is

FURTHER, ORDERED, ADJUDGED and DECREED that J. E. Schecter Corporation is liable to the petitioner Carrier Corporation, in the sum of $9,029.50 with interest from July 30, 1963, for materials furnished in connection with such improvement, and the said petitioner Carrier Corporation is entitled to share in such trust funds in the

amount and extent as aforesaid and J. E. Schecter Corporation is liable to petitioner American Radiator & Standard Sanitary Corporation in the sum of $2,610.00, with interest from July 30, 1963, for materials furnished in connection with such improvement, and the said petitioner American Radiator & Standard Sanitary Corporation is entitled to share in such trust funds in the amount and extent as aforesaid and J. E. Schecter Corporation is liable to Sarco Company, Inc. in the sum of $363.45 with interest from July 30, 1963, for materials furnished in connection with such improvement, and the said petitioner Sarco Company, Inc. is entitled to share in such trust funds in the amount and extent as aforesaid and J. E. Schecter Corporation is liable to Sarcotherm Controls, Inc. in the sum of $176.64 with interest from July 30, 1963 for materials furnished in connection with such improvement, and the said petitioner Sarcotherm Controls, Inc. is entitled to share in such trust funds in the amount and extent as aforesaid, and it is

FURTHER, ORDERED that all other persons having claims for labor or materials furnished to J. E. Schecter Corporation in connection with the aforesaid improvement, and any other reasonable and necessary charge in connection therewith, be given notice by the attorneys for the petitioners to file verified claims with the attorneys for the petitioners on or before September 15, 1965, and on default to be forever barred from making any claim to said trust fund, said notice to be accompanied by a copy of this order, and it is

FURTHER, ORDERED that the debtor furnish to the attorneys for petitioners a certified list of the unpaid claims against such trust fund, setting forth its best available information of the full name and address of each claimant and the amount of its respective claim, within ten days after service of a copy of this order, and it is

FURTHER, ORDERED that petitioners shall serve said notice to file claims and a copy of this order upon each of said claimants by certified mail, return receipt requested, and it is

FURTHER, ORDERED that the following notice be published once in the Long Island Daily Press, a newspaper published in the County of Queens, State of New York, and once in the Princeton Herald, a newspaper published in Princeton, the County of Mercer, State of New Jersey:

"UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

No. 62-B-934

In the Matter

—of—

J. E. SCHECTER CORPORATION,

Debtor.

To:

All persons who have furnished labor or materials to J. E. Schecter Corporation for the erection, construction and completion of the Engineering Quadrangle at Princeton University, Princeton, New Jersey, or any alteration, repair or addition thereto and any other reasonable and necessary charges in connection therewith.

PLEASE TAKE NOTICE that an order has been entered in the United States District Court for the Eastern District of New York impressing a trust on funds in the possession of J. E. Schecter Corporation, debtor, obtained from William L. Crow Construction Company and arising out of an improvement in the State of New Jersey known as the "Engineering Quadrangle",

Princeton University, Princeton, New Jersey, to be applied to the payment of claims of all persons who have furnished labor or materials to J. E. Schecter Corporation for the erection, construction or completion of said improvement or any alterations, repairs or additions thereto, and any other reasonable or necessary charges in connection therewith, and providing for counsel fees to be paid out of said funds to the attorneys for the petitioners, and

PLEASE TAKE FURTHER NOTICE that you are hereby required to present your verified claim to the office of William J. Rudin, Referee in Bankruptcy, 195 Willis Avenue, Mineola, New York no later than the 15th day of September, 1965, and in default thereof you will be barred from making any claim to said trust fund or any part thereof,

SCHWARTZ, WEISSBERGER & LEICHTER
Attorneys for Petitioners
141 Broadway
New York, N. Y. 10006''

and it is

FURTHER, ORDERED that counsel fees shall be paid to Schwartz, Weissberger & Leichter, attorneys for the petitioners, out of said trust funds in an amount to be determined pursuant to a further order of this Court on application by said attorneys at such time as they deem it appropriate and in conjunction with the order of distribution of the trust funds to the beneficiaries thereof at which time a judgment for costs shall be entered in favor of petitioners in a sum to be taxed by the Clerk of this Court.

Dated: Mineola, N. Y., July 29, 1965.

WILLIAM J. RUDIN,
Referee in Bankruptcy.

LIBRARY
SUPREME COURT, U. S.

Supreme Court of the United States

October Term, 1965

No. 463

IN THE MATTER

OF

J. E. SCHECTER CORPORATION,

Petitioner,

AND

CARRIER CORPORATION, AMERICAN RADIATOR & STANDARD SANITARY CORPORATION, SARCO COMPANY, INC. and SARCOTHERM CONTROLS, INC.,

Respondents.

PETITIONER'S REPLY BRIEF

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Supreme Court of the United States

OCTOBER TERM, 1965

No. 463

In the Matter

of

J. E. SCHECTER CORPORATION,

Petitioner,

AND

CARRIER CORPORATION, AMERICAN RADIATOR & STANDARD SANITARY CORPORATION, SARCO COMPANY, INC. and SARCOTHERM CONTROLS, INC.,

Respondents.

PETITIONER'S REPLY BRIEF

Supplemental Statement

The proceedings before the Referee in Bankruptcy, District Court and United States Court of Appeals, substantiated Petitioner's contention that New York State law was not applicable to the instant matter. Respondents have alluded to New York State law in their brief in opposition and therefore, Point II of this reply brief is directed to the applicability of New York State law, with respect to conflicts of law and the Lien Law.

The balance of this brief is submitted as a refutation of the arguments and rationale propounded by Respondents.

In its zeal to do equity, the lower Court transcended the decisions of *Hiller & Skogland, Inc.* v. *Atlantic Creosoting Co.*, 40 N. J. 6, 190 A. 2d 380 (1963); *Plevy* v. *Schaedel*, 44 N. J. Super. 450, 130 A. 2d 910 (1957); *Wasserman* v. *Klahre*, 24 N. J. Super. 143, 93 A. 2d 638 (1952), and the private improvement statutes cited by Petitioner.

Petitioner replies *seriatim* to each of the contentions found on page 13 of Respondents' brief.

POINT I

The Court of Appeals has applied case and statutory law concerning public improvements to a situation involving private construction and private funds.

Respondents' contention that the clear expression by the Supreme Court of New Jersey, in *Hiller & Skogland, Inc., supra,* that civil liability would be afforded the Respondents, is not supported by the decision and is not authority to impress a trust or lien on funds derived by a subcontractor from the construction of a private improvement. The expression by the Court was *dicta,* but in any event, supports reliance by the Petitioner on *Plevy* v. *Schaedel* and *Wasserman* v. *Klahre, supra,* as shown in this brief.

1. Respondents argue that the scope of N. J. S. 2A:102-10 and 11 and *Plevy* v. *Schaedel, supra,* is distinguishable from the case at bar and that no reliance should be placed thereon, indicating that the *Plevy* case was an action involving officers of the corporate debtor, rather than an action against the statutory trustee for an accounting.

The Court's attention is directed to the following specific provision of N. J. S. 2A:102-11, which extends the scope of the criminal statute to officers, directors or agents of the subcontractor who pay or consent to the appropriation of funds, and thus, makes said agents guilty of a misdemeanor and in so doing, extends the definition of statutory trustee to said agents, officers or directors, as well as the corporate subcontractor as recipient of the funds.

> "Any subcontractor, or any officer, director or agent of the subcontractor, who pays or consents to the appropriation of such funds for any other purpose prior to the payment of all claims and charges * * * is guilty of a misdemeanor."

The facts of the *Plevy* case involve a bankrupt corporation, unpaid subcontractors of a private improvement and N. J. S. 2A:102-10 and thus is analogous to the within matter.

2. *Hiller & Skogland, Inc., supra,* is the established law of New Jersey with respect to public improvements and trust funds derived from public agencies. However, the application of the case must be restricted to issues involving public improvements and public funds. A careful reading of the *Hiller* case and the footnote referred to by Respondents does not overrule or distinguish *Plevy* v. *Schaedel, supra,* or *Wasserman* v. *Klahre, supra,* but in reality, and by direct expression of the Court, reinforces in toto the contention of Petitioner herein that the private improvement criminal statute "on its face, is entirely criminal in impact". The exact wording of the Court's dicta was:

> "As to civil liability arising by virtue of the statute, *see* Samuel D. Wasserman, Inc. v. Klahre, 24 N. J. Super. 143 (App. Div. 1952)." (Emphasis supplied.)

Respondents, through innuendo and rationalization, contend that the aforesaid quote reinforces its argument that a trust should be impressed in the instant matter. However, there exists a difference between the term "civil liability" as used in the *Hiller* case, and the terms "trust" or "lien", as employed in the *Plevy* and *Wasserman* decisions. The precise issue involved in the *Wasserman* case was "did a trust or lien arise by operation of law?", and the precise and sole question in the *Plevy* case " * * * is whether or not N. J. S. 2A:102-10 creates a civil remedy * * * ". The issue was not whether civil liability existed for it is axiomatic that an unpaid subcontractor would be entitled to recover for work, labor and services, goods sold and delivered, or breach of contract, and could have enforced its rights under the provisions of the mechanics' and materialmen's lien law of the State of New Jersey. However, no right of action to impress a trust or lien exists under the private improvement criminal statutes or in equity.

The *Plevy* and *Wasserman* decisions are not at variance with *Hiller & Skogland, Inc.*, nor are they at variance with the Legislative history surrounding the enactment of N. J. S. 2A:44-148 and 2A:102-12.

The *Wasserman* decision referred to R. S. 2:124-16 (forerunners of N. J. S. 2A:102-10). The Court, in noting that the two statutes were similar, indicated the following:

> "Under our former Constitution, as under our present one, the title of a statute operates as a limitation on the enacting clauses, so that a construction which would give the statute a direct effect beyond the object expressed in the title must be rejected. Jordan v. Moore, 82 N. J. L. 552 (E. & A. 1912); St. John, etc., Church v. Gengor, 121

> N. J. Eq. 349 (E. & A. 1937). *It is entirely clear to us that the scope of the statutory provision on which the plaintiffs build their case, is limited to the creation of a criminal offense; and that no civil action can be based directly on the statute.*" (Emphasis supplied.)

The "general equity principles" upon which the lower Court made its determination are at variance with the equity decision of *Guise* v. *John C. Guise, Inc.*, 116 N. J. Eq. 590 (E. & A. 1934). The *Guise* decision, rendered subsequent to the passage of N. J. S. 2A:44-148 and 2A:102-12, relating to work performed and materials furnished, occurred prior to the passage of the statutes. The Court refused to give the unpaid claimant any lien on the funds in the hands of a Court-appointed receiver, since no statute had expressly created the right to such relief. The principle of the *Guise* decision, reiterated in the *Wasserman* case, was as follows:

> "In the absence of statute, one who furnishes material or labor for a building or any structure which is part of the land has no lien, legal or equitable, on the land, the structure, or the contract price."

Thus, New Jersey courts of equity have long since recognized that a statute is required before a trust or lien can be impressed on funds due a subcontractor or materialman.

3. The Hiller & Skogland, Inc. footnote contained the following verbiage:

> "This statute, introduced by a different legislator than chapter 268 and 269, had reference only to

> private construction projects and, on its face, is entirely criminal in impact."

There can be nothing clearer from the foregoing to express the awareness of the Supreme Court of the distinctions between the public and private improvement trust fund statutes of New Jersey. The specific reason for the enactment of N. J. S. 2A:44-148 resulted from a 1928 equity case involving *Grover* v. *Board of Education of the Township of Franklin*, 102 N. J. Eq. 415, aff'd 104 N. J. Eq. 197 (E. & A. 1929).

The Hiller & Skogland, Inc. Court reviewed in detail the *Grover* decision, as well as the statutory enactments existing at the time of the determination of *Grover*. The New Jersey Legislature had enacted vast public construction statutes concerning the Municipal Mechanics' Lien Law (N. J. S. 2A:44-125-142), and the Bond Act (N. J. S. 2A:44-143-147) at the time of the rendition of the *Grover* decision. The public improvement trust fund act, in both its civil and criminal counterparts, had not been enacted. The facts of the *Grover* case, as noted by the Court were strikingly similar to the facts of the *Hiller & Skogland, Inc.* case and are presented herein in summary:

> The Board of Education entered into a contract with Stout to build a school. Pursuant to the Bond Act, Stout furnished the necessary surety and purchased materials from Grover. Grover was paid by Stout out of the contract payments received from The Board of Education, but there was no direction by Stout as to how the payment was to be applied. Stout was indebted to Grover on an antecedent indebtedness and Grover knew that the funds received by him from Stout were derived from The Board of Education construction project. Never-

theless, Grover applied the payment on account of the antecedent debt and thereafter filed a lien for the full price of the school materials. Stout abandoned the contract and his surety on the bond completed it.

The issue presented was whether the surety, as subrogee of the contract, was entitled to the balance of the contract price in the hands of The Board of Education, or whether Grover was entitled to apply the funds received from Stout and enforce its lien action under the Municipal Mechanics' Lien Law. The Court upheld the enforcement of Grover's lien, and in effect, required The Board of Education to pay twice, thus reducing the amount collected by the surety as Stout's subrogee.

Thus the Supreme Court had before it the holding of the *Grover* case which, in effect, stated that moneys paid to the contractor by the public body on the contract "became and was his own money—money which he had legally earned, and which belonged to him alone—just as much as any other money he could have". The *Grover* decision would have undoubtedly required the Court to find for Atlantic Creosoting Co., Inc., which stood in the same legal position as Grover, had it not been for the passage of N. J. S. 2A:44-148.

The Court further indicated that:

"Neither the municipal mechanics' lien law, nor the obligation on the contractor created by the bond act required 'either the contractor or the contractor's creditors to make such primary application of moneys received by the contractor on his contract—nothing either expressed or arising by necessary implication'."

The Court, in the *Hiller* case, further stated with respect to the possibility of overruling the *Grover* decision:

> "But we need not go so far in the instant case as to overrule Grover or quarrel too much with the Restatement, because subsequent legislation has nullified Grover's precedential force and indicated a duty falling within the Restatement exception. We refer to the trust fund act, L. 1932, c. 268, which now reads, N. J. S. 2A:44-148."

From the foregoing, it is apparent that the reason for the enactment of N. J. S. 2A:102-12 and 2A:44-148 was the decision of the *Grover* case, rather than the individual requirements of the different legislators who offered the respective private and public improvement trust fund statutes for enactment.

4. The final contention of Respondents relates to the verbiage employed in the respective public and private improvement trust fund statutes. The belabored construction of the statutes by Respondents is not novel and was presented in the *Plevy* case, *supra* (see p. 18 of the petition).

It would appear that the following propositions can be established with respect to New Jersey law:

A. That the Courts of New Jersey have consistently refused to impress a trust on statutory or equitable grounds where the issue involves funds of subcontractors and contractors engaged in private improvements.

B. That the reasons for the enactment of N. J. S. 2A:44-148 was to close a loophole in the Municipal Mechanics' Lien Law and the Bond Act, and the enactment of

said statute was the result of *Grover* v. *Board of Education of the Township of Franklin.*

C. That the decisions of *Plevy* v. *Schaedel* and *Wasserman* v. *Klahre* are not at variance with the decision of *Hiller & Skogland, Inc.,* or the footnote referred to therein, since the Supreme Court of New Jersey has indicated that the private improvements statutes, N. J. S. 2A:102-9, 10 and 11, "had reference only to private construction projects and, on its face, is entirely criminal in impact".

D. There are no cases in New Jersey involving contractors or subcontractors engaged in private construction which have adopted a construction similar to that rendered by the Court of Appeals, nor have there been decisions in New Jersey indicating that the criminal provisions of N. J. S. 2A:102-10 and 11 are also civil statutes affording the aggrieved party the right to impress a trust under equitable grounds or under the statutes themselves.

E. The fact that a bankruptcy court is also a court of equity does not permit that court or any other federal court to transcend the provisions of Title 28 of the United States Code, Section 1652, the decision of *Erie* v. *Tompkins,* 304 U. S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, or the numerous decisions predicated thereon.

F. That a denial of the petition for the issuance of a writ of certiorari in the within matter will upset the established legislation and decisional law of the State of New Jersey, which dates to 1898.

POINT II

The laws of the State of New York are not applicable to the instant proceeding.

A. The laws of the State of New York are not appliable herein notwithstanding the fact that the contract between the Petitioner and Crow provided in substance that its terms and construction shall be governed by the said laws. Although as a general rule of law, parties may contract as to the law governing the contract, this rule is not absolute. The more modern view referred to as the doctrine of the "grouping of contracts" or the "center of gravity" is that the Courts instead of regarding as conclusive the parties' intention or the place of making or performance, lay emphasis rather upon the law of the place which has the most significant contacts with the matter in dispute. *Haig* v. *Barnes,* 9 N. Y. 2d 554, 175 N. E. 2d 441; *Auten* v. *Auten,* 308 N. Y. 155, 124 N. E. 2d 99; *Hausman* v. *Buckley,* 299 F. 2d 696; *Wooten* v. *Marshal,* 279 F. 2d 558.

In *Auten* v. *Auten, supra,* Judge Fuld of the New York State Court of Appeals stated:

> "Choosing the law to be applied to a contractual transaction with elements in different jurisdictions is a matter not free from difficulty. The New York decisions evidence a number of different approaches to the question. See, e. g., Jones v. Metropolitan Life Ins. Co., 158 Misc. 466, 286 N. Y. S. 4.
>
> Most of the cases rely upon the generally accepted rules that " 'All matters bearing upon the execution, the interpretation and the validity of contracts * * * are determined by the law of the place where the contract is made' ", while " 'all matters

connected with its performance * * * are regulated by the law of the place where the contract, by its terms, is to be performed.' " Swift & Co. v. Bankers Trust Co., 280 N. Y. 135, 141, 19 N. E. 2d 992, 995; Union Nat. Bank of Chicago v. Chapman, 169 N. Y. 538, 543, 62 N. E. 672, 673, 57 L. R. A. 513; see, also, Zwirn v. Galento, 288 N. Y. 428, 43 N. E. 2d 474; United States Mtg. & Trust Co. v. Ruggles, 258 N. Y. 32, 38, 179 N. E. 250, 251, 79 A. L. R. 802; Restatement, Conflict of Laws, §§332, 358; Goodrich on Conflict of Laws (2d ed., 1938), p. 293. What constitutes a breach of the contract and what circumstances excuse a breach are considered matters of performance, governable, within this rule, by the law of the place of performance. See Richard v. American Union Bank, 241 N. Y. 163, 166-167, 149 N. E. 338, 339, 43 A. L. R. 512; Restatement, Conflict of Laws, §370; Goodrich, op. cit., p. 293.

Many cases appear to treat these rules as conclusive. Other consider controlling the intention of the parties and treat the general rules merely as presumptions or guideposts, to be considered along with all the other circumstances. See Wilson v. Lewiston Mill Co., 150 N. Y. 314, 322-323, 44 N. E. 959, 961-962; Stumpf v. Hallahan, 101 App. Div. 383, 386, 91 N. Y. S. 1062, 1063, affirmed 185 N. Y. 550, 77 N. E. 1196; Grand v. Livingston, 4 App. Div. 589, 38 N. Y. S. 490, affirmed 158 N. Y. 688, 53 N. E. 1125. And still other decisions, including the most recent one in this court, have resorted to a method first employed to rationalize the results achieved by the courts in decided cases, see Barber Co. v. Hughes, 223 Ind. 570, 586, 63 N. E. 2d 417, which has come to be called the 'center of gravity' or the 'grouping of contracts' theory of the conflict of

laws. Under this theory, the Courts, instead of regarding as conclusive the parties' intention or the place of making or performance, lay emphasis rather upon the law of the place 'which has the most significant contacts with the matter in dispute'. Rubin v. Irving Trust Co., 305 N. Y. 288, 305, 113 N. E. 2d 424, 431; see, also, Jones v. Metropolitan Life Ins. Co., supra, 158 Misc. 466, 469-470, 286 N. Y. S. 4, 8-9; Jansson v. Swedish American Line, 1 Cir., 185 F. 2d 212, 30 A. L. R. 2d 1385; Barber Co. v. Hughes, supra, 223 Ind. 570, 63 N. E. 2d 417; Boissevain v. Weil, (1949) 1 K. B. 482, 490-492; Cook, 'Contracts' and the Conflict of Laws; 'Intention' of the Parties, 32 Ill. L. Rev. 899, 918-919; Harper, Policy Bases of the Conflict of Laws: Reflections on Rereading Professor Lorenzen's Essays, 56 Yale L. J. 1155, 1163-1168; Note, Choice of Law Problems in Direct Actions Against Indemnification Insurers, 3 Utah L. Rev. 490, 498-499.

Although this 'grouping of contacts' theory may, perhaps, afford less certainty and predictability than the rigid general rules (see Note, op. cit., 3 Utah L. Rev. 490, 498), the merit of its approach is that it gives to the place 'having the most interest in the problem' paramount control over the legal issues arising out of a particular factual context, thus allowing the forum to apply the policy of the jurisdiction 'most intimately concerned with the outcome of (the) particular litigation'. 3 Utah L. Rev., pp. 498-499. Moreover, by stressing the significant contacts, it enables the Court, not only to reflect the relative interests of the several jurisdictions involved (see Vanston Bondholders Protective Committee v. Green, 329 U. S. 156, 161, 162, 67 S. Ct. 237, 239, 91 L. Ed. 162), but also to give effect to

> the probable intention of the parties and consideration to 'whether one rule or the other produces the best practical result'. Swift & Co. v. Bankers Trust Co., supra, 280 N. Y. 135, 141, 19 N. E. 2d 992, 995; see Vanston Bondholders Protective Committee v. Green, supra, 329 U. S. 156, 161, 162, 67 S. Ct. 237, 239."

In the instant proceeding it is not the contract which is in question but rather certain rights created by statute. The subject contract was between the general contractor Crow and the Debtor in connection with the improvement of real property in New Jersey. The Respondents were not parties to said contract and have no rights thereunder.

B. Section 70 and 71 of the Lien Law of the State of New York are concerned by their very terms only with funds arising from improvements or contracts relating to real property in the State of New York.

The present Sections 70 *et seq.* of the New York Lien Law are the successors to Sections 36 *et seq.* of said law and are commonly referred to as the trust fund sections.

In *Allied Thermal Corporation* v. *James Talcott Inc.*, 3 N. Y. 2d 302, the plaintiff alleged that (a) New York is the residence of the principals to all relevant contracts and of the diverting parties; (b) the execution of the contracts between the general contractor and the sub-contractor took place in New York; (c) the payment of the trust funds to the sub-contractor occurred in New York; (d) the diversion of the trust fund took place in New York; and (e) the real property which was the subject of the improvement was located in Pennsylvania, The Court of Appeals, in holding that a supplier of material could not use the provisions of the New York Lien Law to force an

accounting for funds received for supplying materials to an improvement of premises located in Pennsylvania, stated as follows:

> "Desmond, Judge. The question is as to whether the language 'for the improvement of real property' in section 36-b of the Lien Law, Consol, Laws, c. 33 (funds received by subcontractor constitute trust funds, etc.) applies to the improvement of real property in States other than New York. Of course, if we read that statute literally and off by itself, there is nothing in it limiting it to subject real property in this State. However, section 36-b must be read as part of articles 2, 3 and 3-A of the Lien Law which constitute New York State's complete scheme for the protection of the rights of those who provide labor and materials for the improvement of real property. At no place in any of the numerous sections which together make up that statutory scheme is there definite reference to 'New York State'. It was, apparently considered so obvious that New York real property alone was involved that it was unnecessary to say so. The phrase: 'for the improvement of real property' which we are here construing in section 36-b recurs over and over throughout these sections. In no place is 'New York State' mentioned but in no place is there any doubt that New York State alone is intended. In fact, when 'real property' is mentioned in any of our statutes there is never a specification that New York real property alone is intended, as witness the definitions in section 2 of the Real Property Law, Consol. Laws, c. 50, subdivision 6 of Section 2 of the Tax Law, Consol. Laws, c. 60, section 40 of the General Construction Law, Consol. Laws, c. 22, as well as in section 2 of the Lien Law itself.

> The purpose of section 36-b of the Lien Law is precisely the same as that of all the other sections in articles 2, 3 and 3-A of that law, that is, to provide special protection for those whose services and materials enhance the value of real property. Since that is the general purpose of all these enactments there seems no reason to single out section 36-b as having to do with the improvement of real property in some other State.
>
> Other States including Pennsylvania (see Martindale-Hubbell, Lawyers' Directory, Vol. III, Digest of Pennsylvania Laws, under heading 'Mechanics Liens') have their own peculiar systems of statutory protections for materialmen and laborers. Only confusion could result from applying one part of a particular State's statutory system to a real property improvement situated in another State where the local statutory scheme is quite different."

In *Allied Thermal Corporation* v. *James Talcott, Inc. supra,* notwithstanding that the applicable provisions of the New York Lien Law in force at that time made no definite reference to New York State, the Court nevertheless held that "it was apparently considered so obvious that New York real property alone was involved, that it was unnecessary to say so". Section 70 of the New York Lien Law went further by specifically limiting itself to improvements of real property in this state.

A lien and any trust fund alleged to flow therefrom, does not exist at common law, is no part of the contract to be enforced, is purely the creature of statute and has no extra territorial effect.

In *Birmingham Iron Foundry* v. *Glen Cove Starch Manufacturing Company*, 78 N. Y. 30, 32, the Court held:

> "Section one of the statute provides that 'any person who shall hereafter perform any labor or furnish any materials in building, altering or repairing any house, building or other improvement upon lands or appurtenances to such house or other building, by virtue of any contract with the owner thereof or his agent, or with any contractor or subcontractor.' etc., shall have a lien. Such a lien does not exist at common law. It is no part of the contract to be enforced where that can be enforced. It is purely the creature of the statute. The statute has no extra territorial force. It was intended for the protection of those who performed labor or furnished materials within this State. When this engine was brought into this State and put into this factory, it belonged to the defendant. The plaintiff did not furnish any material in this State. It cannot, therefore, have the benefit of this statute."

That statutes are to be strictly construed is a well settled rule of law which is more compelling in the case of a statute penal in nature. For example, the former Sections 36-a and 36-b of the Lien Law creating trust funds referred merely to "real property". The courts were not willing to expand the statute to include public improvements. *American Laundry Machinery Co.* v. *Union Trust Co.*, 153 Misc. 55, *Vulcan Rail and Construction Co.* v. *Westchester County*, 250 App. Div. 212. As a result of this construction by the courts, the Lien Law was amended to include "public improvements". Further in order to codify *Allied Thermal Corporation* v. *James Talcott, Inc.*,

the words "in this state" were added to Section 70 of the Lien Law which in its present form states:

> "The funds described in this section received by an owner for or in connection with an improvement of real property in this state, or received by a contractor under or in connection with a contract for an improvement of real property or a contract for a public improvement in this state, or received by a subcontractor under or in connection with a subcontract made with the contractor for such improvement of real property or public improvement or made with any subcontractor under any such contract, and any right of action for any such funds due or earned or to become due or earned, shall constitute assets of a trust for the purposes provided in section seventy-one of this chapter."

Clearly, the trust funds created by the Lien Laws of the State of New York related only to property in this state, regardless of the parties' choice of law relative to the contract, and the New York Lien Law cannot be extended to cover property in the State of New Jersey.

CONCLUSION

It is respectfully submitted that the petition and reply of the Petitioner conclusively demonstrates that the Respondents have no right to impress a trust under the applicable statutes or by reason of equitable principles.

Respectfully submitted,

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